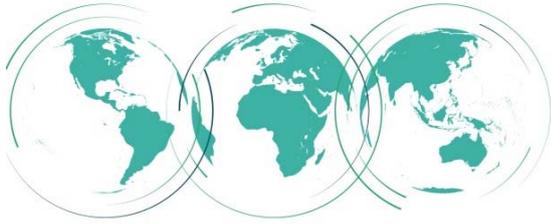


# COUNCIL OF COUNCILS

*An Initiative of the Council on Foreign Relations*



## The Council of Councils Tenth Regional Conference *Panelist Papers*

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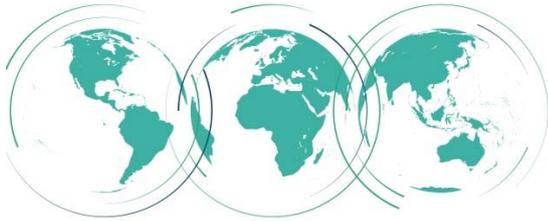
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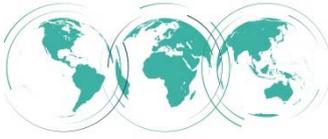
# COUNCIL OF COUNCILS

*An Initiative of the Council on Foreign Relations*



## Session One

### *The Future of the Bretton Woods Institutions: Governance Challenges and Opportunities*



Panelist Paper

## *The Future of the Bretton Woods Institutions: Governance Challenges and Opportunities*

Council of Councils Tenth Regional Conference

November 5–7, 2017

Argentine Council for International Relations, Buenos Aires, Argentina

**Sunjoy Joshi**, Observer Research Foundation

### **Restoring Faith in the Bretton Woods Institutions**

For any international multilateral institution to be credible, legitimate, and effective, it needs to accord equitable status, which is periodically reviewed, to its members. At the heart of the demand to reform the Bretton Woods institutions has been the call for reviewing and redrafting the quotas and voting powers of emerging economies.

In December 2010, the International Monetary Fund (IMF) completed the fourteenth general review of quotas. The package came into effect in January 2016 and is touted as the most far-reaching IMF reform as it significantly realigned quota shares. China became the third largest member country by quota in the IMF, and four emerging market and developing countries—Brazil, China, India, and Russia—are among the ten largest IMF shareholders.

However, a closer look at the reformed quota numbers shows a slightly different picture. The twenty-eight European Union countries together still hold approximately 30 percent of the voting power. Add to this the 16.52 percent voting power of the United States and 6.15 percent of Japan, the majority power at the IMF still resides with the Atlantic system. Brazil, Russia, India, China, and South Africa (BRICS) have a combined share of just over 14 percent.

Another point of contention, which remains unresolved under the fourteenth general review, is the 16.52 percent voting power of the United States. Given any change in quotas must be approved by 85 percent of the total voting power, the United States continues to hold a veto at the IMF. Much of the delay in the implementation of the fourteenth general review of quotas could be attributed to the U.S. Congress, which refused to ratify the agreement.

The fifteenth general review of quotas, the most recent attempt to revise the size and composition of the system, was to be completed by October 2017, but the deadline has now been extended to 2019. The delay and lack of enthusiasm is not unexpected given the precedent set by the 2016 adoption of the previous general review of quotas.

The asymmetric voting power of Bretton Woods institutions is a systemic feature and in many ways reflects the policies adopted by the World Bank and the IMF. The World Bank and the IMF often en-

force loan conditionality based on a predetermined and prescriptive economic model, commonly referred to as the Washington Consensus. This economic model, focusing on liberalization of trade and investment, deregulation of the financial sector, and privatization of nationalized industries, is criticized by many experts, especially in the developed world.

Given that the Washington Consensus was formulated by the same countries that control the Bretton Woods institutions, loan conditionalities often disregard country-specific circumstances, following a one-size-fits-all approach divorced from the experience of emerging countries. IMF conditionalities often result in the loss of a nation's economic sovereignty. Because IMF packages prescribe predetermined national economic policies, they leave little room for negotiation. Developing nations are wary of being compelled to cede their autonomy over domestic economic policymaking to a supranational institution, particularly one where they do not have even equitable voting power. Argentina in the 1990s is a case in point.

Despite the recession in Argentina in the early 1990s, IMF continued to prescribe fiscal surplus and austerity measures, which furthered the economic slowdown, resulting in lower tax revenues. However, since Argentina was liberalizing its markets and integrating itself into the Washington Consensus, the IMF continued to provide economic support. By the end of 1995, Argentina was so indebted to IMF support that any indication of not toeing the IMF line would have resulted in investor backlash.

In fact, during the nineties, IMF prescriptions rarely varied from Mexico and Argentina to Russia and Southeast Asia. And while these conditions enjoyed some successes—Mexico being one such example—they significantly exacerbated adverse conditions largely because IMF prescribed the same response for different problems, such as in Asia that was going through a regulatory and banking crisis and Argentina which was mired in recession.

## **Recommendations**

- Taking into account new geopolitical and geoeconomic realities, the Bretton Woods institutions need to create a more equitable and inclusive global governance architecture. As Indian Finance Minister Arun Jaitley reiterated at the spring meetings of the IMF, further reform of the quota system is needed, lest the legitimacy and credibility of the IMF should further erode.
- The Bretton Woods institutions need to reform not just voting rights but also processes and procedures so that they take into consideration local realities to account for country-specific nuances. In an increasingly globalized world, inaccurate policy recommendations that harm one nation can harm the global economy.

## **Blending the New and the Old**

Assistance from the World Bank and IMF often comes with draconian conditions. The BRICS New Development Bank (NDB) and the Asian Infrastructure Investment Bank (AIIB) were created to act as bulwarks against such perceived exploitation. The emergence of these development banks has provided increased choices for nations to finance development projects. Comprised of emerging economies as member states, NDB and AIIB can also better understand the difficulties faced by developing nations.

This does not mean, however, that the new development banks cannot complement the work of the Bretton Woods institutions. The Bretton Woods institutions have more capital at their disposal than their nascent counterparts, but the NDB and AIIB are likely better suited to understand the nuances of the developed world. An alliance between the regional development banks, utilizing their geographic

and sectoral expertise, and the Bretton Woods institutions, backed by the heft of their capital pool, is possible.

The World Bank is investing \$650 billion into projects such as India's rooftop solar panel program. World Bank could use resources more efficiently if it coordinated with AIIB and NDB to pool the resources of the three banks. Additional funding could be raised by tapping into international private capital in the form of sovereign wealth funds and pension funds. The World Bank, NDB, and AIIB can use this model to significantly increase the number of projects they fund.

Moreover, numerous infrastructure projects currently cannot receive adequate funding due to poor credit ratings. By providing a backstop, multilateral development banks can enhance the credit ratings of these projects and help scale up global infrastructure investments. By pooling their resources together, the World Bank, NDB, and AIIB, could also further the reach of their credit enhancement mechanism.

### **Reimagining Macroeconomic Policy Coordination**

Contrary to common belief, macroeconomic policy coordination has existed since long before the 2007–2008 credit crisis and the subsequent reformation of the Group of Twenty (G20). Central banks across the world have coordinated monetary policy under the Bank for International Settlements (BIS) forum since 1930. However, the numerous financial crises that have occurred since the formation of the BIS make it clear that existing macroeconomic policy coordination is inadequate.

The need for economic policy coordination is evident in a globally integrated financial framework. Economic recessions are no longer restricted to countries and regions, as the most recent financial downturn has shown. Unfortunately, the current geoeconomic governance architecture has only further intensified financial interdependence by applying heterogenic policies across the world. Rather than diversify financial systems based on national and regional specificities, the G20 and BIS have adopted a one-size-fits-all approach that makes global financial systems more susceptible to economic shocks.

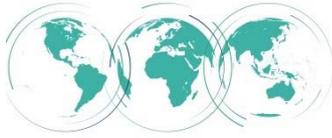
Additionally, the restrictive nature of international regulations such as the Basel guidelines has deterred international investment in the developing world. Stringent capital adequacy restrictions and liquidity requirements have made it costlier for emerging and developing economies to procure private capital flows based on black box sovereign risk assessments and have increased the inequality between the developed and developing nations of the world.

### **Diplomacy to Counter Currency Manipulation**

Nations use currency intervention for various reasons, including but not limited to increasing trade competitiveness. Restricting currency acquisition can prevent nations from managing their foreign exchange volatility or building up strategic reserves, thus harming the global economic equilibrium. Additionally, determining the existence, extent, and motivation of currency intervention can be extremely difficult.

Given these circumstances, it is difficult to imagine a mechanism that could successfully identify and deter trade-based currency manipulation. Placing restrictions on the amount of foreign currency reserves a nation can hold, with accompanying punitive measures for violators, can help. However, negotiating and executing such an agreement would be challenging in the current geopolitical atmosphere.

A more practical response would involve a softer approach, using diplomacy. For example, market forces and multilateral political pressure have deterred China's impulses to devalue the renminbi over the past five years. Similar tactics should be applied to other currency manipulating countries.



Panelist Paper

## *The Emerging Shape of a New Global Financial Architecture*

Council of Councils Tenth Regional Conference

November 5–7, 2017

Argentine Council for International Relations, Buenos Aires, Argentina

**Joseph Chinyong Liow**, S. Rajaratnam School of International Studies

Asia's stock of economic power has been expanding in the last two decades. This has occurred on the back of the rapid and sustained growth of regional economies, not least of which are China and India, whose shares of global trade and gross domestic product (GDP) have increased considerably during this time. If anything, the global financial crisis of 2007–2008 that damaged U.S. and European economies and the anti-globalization sentiments it precipitated rendered the shift of geoeconomic power to Asia even starker.

This shift has begun to have a potentially profound effect on the global financial architecture. The U.S.-led Bretton Woods institutions, the International Monetary Fund (IMF) and the World Bank, have been credited with providing a firm foundation for the post–World War II global financial and economic orders from which Asia and the world have benefited greatly. By the 1990s, however, economic powers such as Germany and Japan, which had both, by dint of having lost the war, failed to acquire preferential decision-making rights in these institutions when they were formed, began agitating for a greater say in the two bodies commensurate with demands for an increase in their respective contributions. These efforts were consistently thwarted by the United States, which sought to maintain its veto rights on all IMF decisions. While Germany did see its position enhanced, albeit obliquely via the tradition of having a European head the IMF, Japanese frustrations led it to create the Asian Development Bank as its major channel of development funding.

By the turn of the century, China and India had emerged as potential Asian economic powerhouses and cast a suspicious eye at U.S. and European dominance of the Bretton Woods institutions. Mindful of Japan's failure to increase its influence in these institutions, the discourse on global financial architecture and governance began gradually to move beyond the matter of internal reform of the Bretton Woods institutions toward the creation of new institutions. This shift in discourse would soon bear fruit. These efforts first found expression with the Japanese proposal for an Asian Monetary Fund after the Asian financial crisis, an initiative that could not take off as a consequence of U.S. opposition. It nevertheless paved the way for what would come later, in spirit if not in form: first, the idea of a BRICS (Brazil, Russia, India, China, and South Africa) development bank and, later, the Asian Infrastructure Investment Bank (AIIB). Unnerved by the IMF's role during the Asian financial crisis, the Association of South East Asian Nations (ASEAN) also created its own regional crisis response mechanism, the Chiang Mai Initiative Multilateralization, to perform functions similar to the IMF but

with a regional flavor and in coordination with ASEAN's Plus Three partners: China, Japan, and South Korea.

What accounted for the emergence of these alternative institutions?

First, while the Bretton Woods institutions may underpin the global economic order, they have also proven notoriously difficult to reform to more accurately reflect the global shift in economic influence. Until recently, Asia's share of global GDP and its share of the IMF quota, which affords member countries a say in the governance of the international financial institution and, by extension, the global financial architecture, had been acutely misaligned. In 2010, the IMF executive board had already agreed to proposals for institutional reform to redistribute quotas away from the traditional economies to the emerging economies. Even so, because the United States holds the largest share of voting rights, effectively affording it a veto, it took another five years to secure U.S. congressional approval, and only after extensive lobbying of reticent Republicans by the Barack Obama administration. As a result of these reforms, China received the largest quota share increase—more than 2 percent—moving it from sixth to third largest contributor. Even so, this increase is hardly commensurate with its growing economic heft. The IMF also moved in October 2016 to include the renminbi in its basket of special drawing rights (SDR) currencies, but influence on the executive board still remains largely in American and European hands.

Second, because of this misalignment between Bretton Woods governance structure and geoeconomic realities, emerging economies could be reluctant to privilege mechanisms controlled by the United States or Europe should a new crisis erupt. Not to put too fine a point on it: when the IMF coerced the Suharto administration in Indonesia into adopting structural adjustment policies at the height of the Asian financial crisis, it essentially sent an already desperate situation into a tailspin. It was precisely regional reservations toward the IMF's role during this crisis that prompted the creation of the Chiang Mai Initiative Multilateralization.

Third, the emergence of an alternative global financial architecture expressed in the form of BRICS financial institutions or the AIIB is to some extent also an inevitable consequence of structural forces generated by the accumulation of reserves by China, India, and other emerging economies, whose growth rates in the past two decades have outstripped those of the developed economies. As reserves exceed domestic demands for loans in these crucial emerging economies, they are recycled to other parts of the world. Of course, the downside of relying on excess domestic reserves is that the efficacy of these nascent institutions will be dependent on continued sound performance of the economies where the reserves are invested.

Fourth, there is one common, unmistakable thread running through all these institutions: the role of China. By virtue of being the main financier of the BRICS development bank and the AIIB, China's role in this new financial architecture has been paramount. Alongside these institutions stands President Xi Jinping's flagship project, the ambitious Belt and Road Initiative (BRI), envisioned to enhance connectivity and infrastructure development across Eurasia while also addressing the need for development in China's western regions. Indeed, if there was any doubt that China harbors aspirations to play a leading role in geoeconomics as a provider of international public goods, it would surely have been put to rest by Xi's speech at Davos earlier in 2017 and in his address at the Nineteenth Party Congress of the Communist Party of China.

Finally, the Bretton Woods institutions have also faced heavy scrutiny in the Western countries in which they originate. Their controversial policies on austerity in Europe have elicited visceral responses from both the left and right, contributing in no small part to conditions that have given rise to anti-globalist populism in their own backyards. While Asian societies would be well advised not to consider themselves immune to these forces, it is nevertheless this present manifestation of populism in the West that has generated internal pressures on these institutions and hastened concern that the growing criticism needs to be addressed with urgency.

All this is not to say, however, that these Bretton Woods alternatives are risk-free or that they are bound to succeed. BRICS as an arrangement has faltered over the mixed economic performance of some of its members in recent times. Moreover, many of these alternative institutions are, as yet, untested, given that most of them emerged after the global financial crisis. Indeed, they may yet prove ill-equipped in times of future crisis or no less effective than the Bretton Woods institutions. In any case, it is more likely that these alternative institutions will work in tandem with the IMF and World Bank rather than replace them. Notwithstanding these uncertainties, the establishment of these institutions indicates that, even with internal reforms, the World Bank or IMF will likely not remain the primary port of call in times of future storms.

With this diffusion of economic power and the emergence of these new institutions, the shape of the global financial architecture has changed. Correspondingly, the clout of the Bretton Woods institutions—and by extension the United States' soft power reach—will diminish. In fact, the historical coincidence of the rise of these new configurations of economic power together with the United States' inward turn and Europe's continued malaise suggests the emergence of a new multipolar order and a decentralized global architecture in which the Bretton Woods institutions and regional institutions should complement each other in providing global public goods. Such opportunities for collaboration on grounds of complementarity can take the form of better coordination of in-country financing efforts, sharing of information and analysis among respective specialists in both sets of institutions, and U.S. and European involvement with AIIB and participation in BRI projects.



Panelist Paper

## *What Is Wrong With the IMF and How to Fix It*

Council of Councils Tenth Regional Conference

November 5–7, 2017

Argentine Council for International Relations, Buenos Aires, Argentina

**Bessma Momani**, Centre for International Governance Innovation

### **IMF Reforms**

Those advocating for International Monetary Fund (IMF) governance reform widely agree on prioritizing the recalibration of quota shares and voting power. This agreement reflects the sentiment that the IMF will continue to face crises of legitimacy unless it creates governance structures reflective of and adaptive to changing political and economic realities. The fallout of the 2008 financial crisis was a case in point, showing the disconnect between shifting global power dynamics and IMF governance. Developing and emerging market countries, such as China, were given little institutional governing power but were called on by the IMF to shore up their finances and help mainly eurozone countries. To meet its members' needs, the fund must address the potential crisis of legitimacy ensuing from a governance structure that does not adequately reflect global economic power distribution. Thus, calls for recalibration of quota shares and voting power in the fund are as valid as ever.

The IMF has instituted changes in quotas and voting power to reflect changing political and economic realities in the past, but these tend to take long to materialize and require a great deal of politicking. At the IMF's founding, for example, the U.S. quota share was more than 30 percent of the total votes; in 2016, it was 16.6 percent. Although the United States has often given up most of its quota share and voting power to allow more countries into the fund's governance structure, it has kept its veto by staying above 15 percent of quotas and voting power on most issues. Historically, quota and vote changes have reflected political bargains rather than economic realities. The United States is in fact underrepresented in terms of its relative weight in the global economy, which stood at approximately 22 percent in 2013. Nevertheless, the IMF's decision-making rules still allow the United States to maintain a great deal of power at the fund, including its veto at the executive board.

The irony of the U.S. veto, as noted by Wade and Vestergaard, is that it was intended to allow the United States to lead the IMF when other countries were at an impasse.<sup>1</sup> Yet because changes to IMF quotas and executive board composition require U.S. congressional support, many critical issues remain at the mercy of the U.S. Congress even when the rest of the world (not to mention U.S. leadership, as was the case under President Barack Obama) has reached a consensus.<sup>2</sup> This has led some members to seek to eliminate the U.S. veto. While the U.S. veto was ultimately maintained after the 2016 approval of the Fourteenth General Quota Review (U.S. Congress finally granted its approval, possibly in response to such debate over being circumvented), it might be the time for the United States to consider changing

the supermajority rules that allow it to have a veto in the first place. As Wade and Vestergaard point out, with continued ad hoc increases in quotas and voting, China could eventually achieve enough quotas to also have veto power.<sup>3</sup> The authors speculate that it would be in U.S. interests to abolish the supermajority rules, as that would block China from achieving a veto and would allow the United States to use its structural power to influence other countries to support its leadership.

To its credit, the IMF has recalibrated its quota allocation and voting share to more accurately reflect the economic realities of the early twenty-first century. European voting power has been reduced, and China is now the third-largest member country in the institution. Brazil, India, and Russia have also seen significant gains in their voting power. Still, low-income countries have managed only to maintain their voting shares, not enhance them. Another area in which the chasm between IMF word and deed has closed involves the elimination of appointed executive directors. As of 2016, all executive directors, even those from the largest member countries, must be formally elected.

Yet, despite these moves, the IMF's legitimacy continues to be undermined by its unwillingness to replace the informal process of selecting its managing director. An effective twenty-first-century IMF needs to reject the tradition of de facto European managerial leadership. This is particularly salient given the IMF's commitment to the Sustainable Development Goals, which put greater institutional focus on the global south.

Another area of IMF governance that remains problematic is the United States' continued ability to unilaterally veto any IMF decision. As documented by IMF scholars, the United States has politicized IMF decision-making. Any nation state given the same power, including China, would likely rationally pursue similar behavior. There is one option that would maintain executive board coherence: elimination of the 85 percent rule for select decisions. This would allow economically powerful states such as the United States or China to maintain appropriately large voting power but undermine their ability to unilaterally politicize IMF decision-making.

### **Increased Coordination Needed**

In the autumn of 2008, the global financial system began to collapse. What began as a series of failures involving obscure U.S. investment vehicles unleashed chaos across the U.S. financial sector. The crisis soon went global, as investors began to reassess the sustainability of the rapid credit growth that had occurred throughout the developed world in the preceding half decade—particularly in the United States, United Kingdom, and eurozone periphery. Before long, even emerging market economies were drawn into the crisis. While the immediate cause of the crisis was the collapse of the U.S. shadow banking system and the housing market bubble it had spawned, these were symptoms of broader flaws in the financial sector. There was, above all, a misplaced presumption of the inherent efficiency of system coherence.

The international financial crisis exposed significant gaps in the global financial architecture. The severity of the crisis spurred policymakers to undertake calls for increased knowledge sharing, working across institutional boundaries, and strengthening coordination. The Group of 20 (G20) and many governments called for the IMF to take part in efforts to improve global policy coherence among and across international economic and financial institutions; some even noted that the international financial crisis could have been prevented or minimized had there been better communication and transparency of financial flows between states and markets. A lesson of the crisis is that the IMF needs to com-

mit to more consistent collaboration with other intergovernmental organizations and even nongovernmental organizations (NGOs). Most pertinent to the IMF's work is its relationship with the World Bank, but newer organizations such as the Asian Infrastructure Investment Bank (AIIB) are also significant. Indeed, while the IMF and World Bank make efforts to work on joint projects, a surprising degree of mistrust and poor communication exists between the two institutions. Greater institutional attention to building bridges between the IMF and World Bank is thus in order.

Global economic challenges will continue to be relevant. The IMF has historically seen itself as a leading international economic organization that covers monetary, fiscal, and exchange rate policies. As the fund mandate has crept into areas of inclusive growth and global poverty, it has begun competing for space with organizations such as the World Bank and other regional banks, and with the Financial Security Board (FSB), which the G20 created and empowered with more resources and tools to help predict and diagnose faults in the financial system. With respect to the fund's surveillance role, the IMF's increased integration with the G20 and its work with the FSB are positive steps in the post-2008 period. In this era, the IMF simply cannot do it alone, but its willingness to collaborate with other organizations is uncertain. Moreover, as the creation of the AIIB demonstrates, the IMF's powerful members do not always agree on how to govern the global economy. The AIIB could be a valuable contributor by providing IMF members with added capital for important infrastructure projects, but, as the history of the failed Asian Monetary Fund shows, the IMF's most powerful backers may not want to see other organizations spring up and compete with the fund's global lending supremacy.

Systemic trends in global governance and the global economy indicate that the IMF will need to increase its collaboration with other international organizations and NGOs. The fallout from growing critiques of the IMF, from the late 1990s to the Asian crisis and on to the recent international financial crisis, has led to powerful calls to increase interinstitutional coordination. Despite political risk due to U.S. misgivings, the fund should seek to build a meaningful relationship with the AIIB. Although the AIIB has been accused of trying to supplant the Bretton Woods organizations or undermine the liberal world order, it is better seen as a complementary organization. As Perlez notes, the AIIB is focused solely on funding infrastructure projects, such as airports, bridges, and roads, whereas the World Bank's chief mandate is poverty reduction.<sup>4</sup> Moreover, the developing countries in Asia face a shortage of capital available to finance and invest in infrastructure development. Nevertheless, the AIIB has a broader membership base than the Asian Development Bank (ADB) and has greater potential to raise financial resources. It is clear that some of China's drive to create the AIIB was linked to the slow pace of reform at the IMF and World Bank and the failure to give China and other emerging market economies a greater voice and vote on the executive board. The desire to create the AIIB also stems from China's frustration with the IMF conditionality that has followed what China believes are dogmatic prescriptions.<sup>5</sup> That said, the AIIB cannot compete with the Bretton Woods organizations in scale of capital resources or in staff capacity. On capital alone, the AIIB is dwarfed by the IMF, ADB, and the World Bank. On staffing, the AIIB should hire globally to acquire the kind of local knowledge and expertise required to give sound economic advice and assess creditworthiness.

Finally, some have speculated about the implications of this move for enhancing China's future leadership in global economic governance institutions; others have outright declared the multilateral bank a notable indicator of U.S. decline.<sup>6</sup> The AIIB is still in its infancy. If the United States retreats from global affairs and becomes more unilateralist under President Donald J. Trump's administration, China could claim some moral leadership in the global economy. Notably indeed, Chinese President Xi Jinping spoke at the 2017 World Economic Forum defending economic globalization and international coop-

eration on issues that threaten global prosperity and growth. This contrasted with the populist-nationalist tone of the Trump administration, which claims an unfair advantage built into the global economy's rules of the game, rules that have paved the way for U.S. dominance. Xi heralded the Belt and Road Initiative (BRI) as an ambitious foreign aid program that will bring investment, economic growth, and open trade routes to developing markets. He declared that China is open to trade and invited the world to take advantage of its market, the largest developing economy in the world, just as the United States is expected to raise protectionist barriers and break down free trade agreements.

### **Promoting Involvement and Accountability With Civil Society**

As an integral part of the global financial and monetary architecture, the IMF should seek to promote the best possible practices in its work with civil society organizations (CSOs). Citizen scrutiny of government policies can promote government accountability and transparency, and it is a cornerstone of good governance. But with the rise of global populism comes the risk of backlash against international organizations that particularly advance liberal international trade.

As the IMF and other international financial institutions have called on governments to practice good governance, NGOs have called on global institutions to similarly promote involvement and accountability with member states' citizens. The IMF has already determined that successful financial programs are predicated on country ownership. When combined with members' sound economic policies, citizen-led accountability mechanisms can deepen good governance and ensure that economic recovery and growth are enjoyed by a broad spectrum of society.

In the past decade, the fund has made great strides in strengthening its outreach activities. In keeping with findings of academic and external studies, IMF staff have been increasingly more open to consulting with a wider group of actors than in previous years. Some of this is attributable to a more humbled staff after the international financial crisis and to a modest cultural shift within IMF staff toward listening to outside ideas and views. There remain, however, opportunities to further improve staff strategies for working with NGOs.

Despite the observation in numerous interviews with IMF staff that many were not aware of the *Guidelines for Staff Relations with Civil Society*, there appears to be a genuine interest and desire among staff to improve program design and to reach out to a broad spectrum of actors.<sup>7</sup> It was observed that many fund staff, however, may not have the requisite toolkit and internal organizational support to carry out an effective exercise: time demands on staff are extremely high, staff do not receive necessary training, and staff cannot depend on learning from the experiences of more senior staff. The fund should invest in ensuring that it better works with CSOs to both strengthen country ownership of its reform policies and to bring in citizen-based accountability into its loan programs.

*This paper uses excerpts from Bessma Momani's upcoming book, What's Wrong With the IMF and How to Fix It, to be published by Polity Press in December 2017.*

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# COUNCIL OF COUNCILS

*An Initiative of the Council on Foreign Relations*

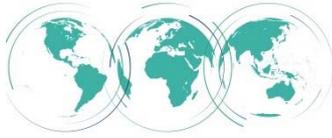


## Session Two

*What Can Be Done to Reverse the  
Fade of Liberal Democracy?*

# COUNCIL OF COUNCILS

An Initiative of the Council on Foreign Relations



Panelist Paper

## *Back to the Grand Debate*

Council of Councils Tenth Regional Conference

November 5–7, 2017

Argentine Council for International Relations, Buenos Aires, Argentina

**Slawomir Dębski**, Polish Institute of International Affairs

### **The Liberal Paradox**

Liberal democracy needs to admit that its own ideals and institutions might be turning against it. Liberalism is, at its core, optimistic about human nature and the prospects for the progress of humankind. Therein, however, lurks a dangerous allure: if progress is inevitable and only natural, then the methods that are meant to bring it about can be considered an afterthought, because it does not really matter how one gets closer to an already known destination.

One such method that believers in a predestined progress often resort to is to blame and shame those who do not share their enthusiasm, thus putting them on the sidelines of the debate—the backbone of any democratic decision-making process. Indeed, progress cannot be achieved without a candid assessment of past experience, including mistakes and missteps made by those in power. Throughout history, those who felt disenfranchised—because of their ancestry, wealth (or lack thereof), or social (class) status—often reached a tipping point and revolted, bringing about progress with distinctly undemocratic means. Absolutism, no matter the derivation, had never had a better or more competitive offer when confronted with the instincts of progress, and thus, as a rule, had to cave in.

One wonders if political correctness—the shield used in a democracy to defend its achievements and to supposedly streamline, or simply limit the debate—presents a new kind of absolutism, claiming that there are issues that cannot or need not be part of the critical, open discourse, because progress is irreversible. Or if humanity is confronted with a new kind of disenfranchisement, this time of those who believe that the kind of progress that humankind has achieved so far is not perfect and ought to be accounted for. If this was the case, then such a paradox ought to lead to a candid conversation about the basics of democracy and the responsibilities of elites in a democratic state.

### **Democracy as Self-Regulating**

The mechanism of democracy is self-regulating; it invites different, conflicted views, which are mitigated in a consensual process. Democracy, by nature, invites different opinions, safeguards minorities, looks for the common denominator. But it does not allow for a violent revolution, the kind of a turmoil history witnessed in France of 1789 and Russia of 1917.

In the simplest definition, it is a way to remove a government without bloodshed. Violence is banned from the democratic process. Yet, eradicating violence does not mean removing conflict, which in essence is the daily bread of democracy. Conflict can be resolved peacefully as long as power is legitimized. Legitimization comes from the conviction of the people that they are ruled over justly.

### **The Responsibility to Convince**

One major conclusion from the reflections on democracy is that diversity is its linchpin. Conviction is a necessary element of the democratic toolkit because it facilitates the grouping of opinions. A political party, especially one that has claims to power, cannot afford to be just a representative of a one-view group. It needs to rally groups with various opinions. That is why convincing is a necessity.

The elite, including intellectuals, has given up on the art of explanation and conviction. Emotions have gotten the better of debates. Emotions create a black-and-white division, a zero-sum game, which divides societies, decertifying a broad margin of legitimate views. The natural social diversity, however, creates many more than just two camps. In every society, no matter how big, these are manifold.

### **International Relations as Democracy on Another Level**

In its majority, the democratic world is a representative democracy, which burdens the representatives and the elites with a task of educating and convincing. In a complex world, where even buying bread is a complicated matter, the power of explanation cannot be underestimated.

In international relations, the great debates of the nineteenth and twentieth century sadly belong to the past. No longer are the advantages of the Wilsonian idealism or the drawbacks of Kenneth Waltz's realism discussed. The global liberal elite has given up on arguing for the liberal order altogether as if it was self-explanatory. New generations, empowered by democracy but unaware of the root causes of the principles that the liberal order abides by, are tempted by the allure to dissent. Dissent they can, but—if they do not become involved in the debate about systems, orders, and the underlying principles—they will not know the red lines, which when crossed could lead to the darkest moments in human history.

### **Back to the Grand Debate**

In 2018, the Atlantic world will celebrate the hundredth anniversary of the Fourteen Points of Woodrow Wilson. The Wilsonian idea is of international relations as a business of equals, thus guaranteeing peace. The concrete debate that this anniversary could initiate is about what remains of Wilson's idea in today's world order: if tribalisms and separatisms are the remains of the Wilsonian idea of self-determination or whether they go against the association of nations and peace altogether; or if there truly is an equality of trade conditions or whether some are more equal than others; or if colonial claims have been adjusted.

The Council of Councils is the right forum to go back to the basics and launch a global debate on principles in international relations, their origins, history, and results. Experts spend time in highly specialized seminars taking basics for granted. That could be one of the reasons why these fundamental principles are being challenged.

# COUNCIL OF COUNCILS

An Initiative of the Council on Foreign Relations



Panelist Paper

## *What Can Be Done to Reverse the Fade of Liberal Democracy*

Council of Councils Tenth Regional Conference

November 5–7, 2017

Argentine Council for International Relations, Buenos Aires, Argentina

**Michael Fullilove**, Lowy Institute

There are at least four questions to consider: whether liberal democracy is really fading; how the challenge to liberal democracy affects global cooperation; what societies can do to ameliorate political polarization and the attack on liberal democratic values, and what can be done to bolster these values in the international sphere

### **Challenge to Liberal Democracy**

Clearly, vast impersonal forces are at work enabling these challenges to liberal democracy. The extremely rich and the extremely poor have done well since the end of the Cold War but the middle of the income distribution has stagnated. And a weariness pervades the West: Iraq and Afghanistan hurt its confidence and the global financial crisis hurt its prosperity.

To a historian, individuals matter. Leaders make decisions that make history. If Hillary Clinton had run a better campaign in 2016, then current discussions would probably be about the triumph of insiders and the durability of the major parties. Had David Cameron not put EU membership up for decision at a referendum and had Boris Johnson not supported the Leave side, then the United Kingdom would probably not be exiting the EU.

That said, something different is clearly happening in international politics. A cohort of nationalist strongman leaders in China, Iran, and Russia are presenting significant challenges to liberal democracy and the liberal international order. Recent years have also seen the rise of political figures with illiberal tendencies in free democracies, including Viktor Orban in Hungary, Recep Tayyip Erdogan in Turkey, Nicolas Maduro in Venezuela, and Rodrigo Duterte in the Philippines. Populist candidates surged this year in France, Germany, and the Netherlands as well but fell short of victory. Something important is happening—but it has been enabled by some very poor decision-making by leaders. If bad decisions caused this change, then perhaps good decisions can help reverse it.

### **The Effects of the Challenge to Liberal Democracy on Global Cooperation**

The link between these politicians is a tendency toward insularity. In many countries, the political divide is increasingly not between left and right but between open and closed. These illiberal figures see free trade as a barrier to prosperity, not a bridge to markets, investment, and ideas. They define their

interests narrowly and are allergic to international cooperation.

Donald J. Trump is the most important example, because the United States is involved in every element of international cooperation. There is a demonstration effect when the leader of the free world does not believe in the free world. Trump's foreign policy instincts are sharply different from those of his predecessors. He is not persuaded that the United States does well when others do well; in fact, he seems to prefer that others do poorly. He is contemptuous of international institutions that, for the most part, serve a useful function for the United States. As Trump said in his speech to the United Nations: "I will always put America first, just like you, as the leaders of your countries, will always and should always put your countries first."

### **Actions to Take at Home**

Democracies also face the issue of political polarization. The rise of new media has not made people any wiser or more enlightened. The relentless pace of the news cycle has reduced their patience. The tone of public debate has soured. Arguments on social media are often personal and quick to escalate.

It goes without saying that political leaders should use social media in a way that encourages respectful public debate, but that is not guaranteed. The Lowy Institute recently hosted Bret Stephens, the conservative *New York Times* columnist, who delivered a lecture entitled "The Dying Art of Disagreement." He called disagreement "the most vital ingredient of any decent society."<sup>1</sup> We have rarely disagreed more, Stephens argued, but we have lost our capacity to disagree well: "To disagree well, you must first understand well. You have to read deeply, listen carefully, watch closely. You need to grant your adversary moral respect, give him the intellectual benefit of doubt, have sympathy for his motives, and participate empathically with his line of reasoning. And you need to allow for the possibility that you might yet be persuaded of what he has to say."

That does not describe the current state of public debate in most liberal democracies. Individuals and institutions such as the participants of the Council of Councils regional conference, have an important role to play in reforming public debate. Nonpartisan, fact-based analysis is the antidote to the spread of propaganda and disinformation.

### **Actions to Take Abroad**

The travails of Western democracies and the rise of illiberal leaders have an implication on foreign policy. As Aaron Friedberg argued in his book about the latter days of the British Empire, *The Weary Titan*, hegemons and powerful states tend to create an international order based on their domestic political systems. For middle powers in 2017, this is particularly concerning.

Liberal democratic principles informed the liberal international order which has, for the most part, provided stability for nearly three-quarters of a century. The order is defined by shared norms such as democratic government and economic liberalism, and is embedded in alliances, agreements, and multilateral institutions.

The United States has always sat at the center of the liberal international order. Now, however, it has a president who is neither liberal in his outlook nor international in his posture or orderly in his behavior.

Domestically, his response to white supremacists marching in Virginia troubled liberals everywhere.

“Charlottesville” became shorthand for racism, violence, and a president’s moral blindness. Externally, Trump wants the United States to play a shrunken role in the world. He is sympathetic to isolationism, and skeptical of alliances. He is hostile to free trade. He swoons over autocrats and strongmen.

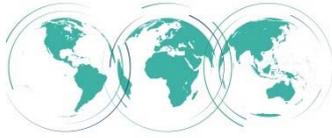
At a time when challengers are on the offensive and some liberal democracies are being led by illiberal individuals, countries like those represented on the Council of Councils should do more to strengthen the liberal international order and the values that inform it until this fever passes.

My own country, Australia, should adopt a larger foreign policy. It should work as closely as possible with its long-standing ally, mainly by working with other partners in Washington rather than relying on the president himself. But it should also strengthen its ties with Asian democracies such as India, Indonesia, Japan, and South Korea. Greater cooperation with like-minded regional powers can be an important hedge against the dual hazards of a reckless China and a feckless United States.

Seventy years ago, the Harry S. Truman administration helped create the postwar world. Truman’s Secretary of State Dean Acheson called his memoir *Present at the Creation*. Today, we might be present at the destruction.

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1. Bret Stephens, “The Dying Art of Disagreement,” speech delivered at the Lowy Institute, September 23, 2017, <http://lowyinstitute.org/publications/dying-art-disagreement>.



Panelist Paper

## *The Demise of Liberal Democracy*

Council of Councils Tenth Regional Conference

November 5–7, 2017

Argentine Council for International Relations, Buenos Aires, Argentina

**Fernando Petrella**, Argentine Council for International Relations

The current difficulties of the liberal international system can be seen mostly as a necessary by-product of domestic liberal democracy.<sup>1</sup> Liberal democracy—as the most effective tool to organize domestic societies—was consecrated in the West as a result of World War II under the influence of the United States and its allies. Its main values were more or less reflected in the Organization of American States (1948), the UN Charter (1945), Bretton Woods institutions (1944), and the human rights covenants (1966).

For a long period of time, under the umbrella of these institutions, the international system was able to manage problems concerning the East and the West, including the Cold War; containment of the Soviet bloc; promotion of decolonization of countries and peoples; and conclusion of the Treaty of Tlatelolco on Denuclearization of Latin America (1967), Non-Proliferation Treaty (1968), Stockholm Convention (1972), and the Helsinki Accords between the United States and the Soviet Union (1975), while providing room for the Non-Aligned Movement, an expression of a sort of “neutrality” apart from the East and the West, embraced by many countries of recent independence. This period also saw the emergence of personalities such as John F. Kennedy, John Paul II, Vaclav Havel, Lech Walesa, and Mikhail Gorbachev.

It is relevant to indicate that most of the above-mentioned documents were signed by a minority (approximately 54 countries) among the 193 UN members of 2017. Due to this arithmetic fact, the coincident view in domestic and external affairs stemming from the end of World War II is no longer exists, and neither is the Soviet “empire” that provided cohesion to the West. The equation of power is in the process of changing but nobody can predict what is going to come out from the present disarray.<sup>2</sup>

Of the new elements that are altering the domestic and international system, bringing about the demise of liberal order in this scenario of irreversible globalization, the more relevant ones include domestic inequality, terrorism, free trade versus protectionism, climate change, and the disregard for international law and the rules of global governance. On top of that, one can add the “rise of the rest.”<sup>3</sup>

- Domestic inequality is the most disruptive, because it dramatically affects the internal social contract. Regarding the need to tackle inequality, Ronald Inglehart summarizes the issue, saying “Today the conflict is no longer between the working class and the middle class; it is between a tiny

elite and the great majority of citizens.”<sup>4</sup> The crucial question is how and when that majority develops a sense of “common interest” and action.<sup>5</sup> Due to the complexity and dire implications of this problem, politicians tend to look elsewhere to assign responsibilities (China is to blame! It’s Germany! It’s Brussels! Look at Mexico! The UN is useless!), and mistrust and resentment spread into the international environment. Causes of inequality are numerous, stemming from the growth of a financial economy, rapid innovation and globalization that affect job creation, and the ability of some individuals and communities to exploit the opportunities that capitalism affords.<sup>6</sup> Neglecting to take action to restore hope to those who can no longer share in the proverbial cake (taxation, redistribution, financial transparency, universal insurance, etc.) clearly endangers the liberal internal and international order as designed and conceived by the West.

- A second element of disruption is terrorism. Countering it requires, as a first step, a radical change of opinion among some European intellectuals that, in the past, influenced governments to sympathize with terrorism in Latin America and in the Middle East active in killing innocent civilians during democratic regimes. The image of Che Guevara and the bloody Guevarista experiment was revered in countries that now have to face the scourge of terror. Fortunately, the 1960s and the 1970s were a long time ago, Cuba is different, and governments and international institutions established a set of rules to deal with this tragic phenomenon. From the UN Security Council Resolution 1373 (2001) onward, the legal framework is clear: Terrorism is a crime against humanity that endangers peace and security and has to be combatted by “all means,” without impinging on fundamental liberties.<sup>7</sup> Yet, the battle against terrorism and its cultural fundamentals is not easy. It requires early and constant education against terror, the visibility of the victims—never to be suppressed or ignored—and victims’ cooperation and commitment no matter the risks involved. But terrorists should also be held accountable, rather than killed on the spot and made into martyrs (as in Barcelona in August 2017), and brought openly to justice to convey an unequivocal message that individual terrorists will never be condoned and their crimes will never be prescribed. The great challenge is to achieve a balance between judicial efficacy and the human rights of the perpetrator and accomplices. In the field of ideas, a balance between political correctness and genuine determination is necessary.<sup>8</sup>
- Strong discussions arose recently between supporters of free trade and those of a revival of protectionism. This debate is related to the idea of isolationism and fragmentation versus globalization and integration. The Donald J. Trump administration fueled the idea of isolation and fragmentation when it criticized the North American Free Trade Agreement (NAFTA) and the Trans-Pacific Partnership (TPP). Trump prompted a vigorous reaction in Davos, the Group of Twenty (G20), and the United Nations General Assembly.<sup>9</sup> China, Germany, and the United Kingdom are strong supporters of free trade.<sup>10</sup> Free trade is a great progress from crude socialism. It promotes friendly relations among governments and influential elite groups based on common benefits. Yet, it is not so clear if unchecked economic liberalization is a real panacea, since it is not immune to bringing about adverse distributional consequences for the majority of people.<sup>11</sup> Hence, more inequality knocks at the door. Sudden isolationism and fragmentation, as proclaimed by the Trump administration, leaves political allies and trading partners out in the rain looking for new partners whose ideas, vis-à-vis the liberal consensus, could be different. Ruling by military threats and the use of force only, leaving aside soft power, active diplomacy, and financial capacity to assist friends, is a serious mistake. To believe that foreign policy is tantamount to conducting business at home is also a mistake. Mistakes like this weaken trust in the liberal international order, because they make liberal democracies appear incapable of protecting and assisting historical allies and friends.

- Early in the seventies, Peccei and Sallustro, two Italian entrepreneurs, published *The Limits of Growth*, the painter Garcia Urriburu unveiled his ecological manifesto in Venice and Paris, and a new awareness about environmental deterioration clicked at the United Nations.<sup>12</sup> The Stockholm Conference took place in 1972, followed by the Rio Conference (1992), Kyoto I and Kyoto II (1992 and 2013), and now the Paris Agreement (2016). Many years elapsed with poor results. Fortunately, the Paris Agreement, despite a few flexibilities, is operative and widely accepted. The European Union is already enforcing it and, hopefully, Trump is leaving the door open.<sup>13</sup>
- Finally, there seems to be a disregard for international law and international rules. The domestic liberal order is based on the respect of democratic rules and so is the international liberal order. It requires a global order anchored in active diplomacy among states and nonstate actors to find solutions through compromise. The international liberal order discourages unilateral use of force and relies on international law and institutions. It does not pursue uniformity. Yet it needs a minimum understanding of human rights and fundamental freedoms to be practiced by the main power holders.<sup>14</sup> Neglecting international law and rules of global governance, in a period of accelerating globalization and diffusion of power, is another serious mistake.

Fading liberal democracy is linked to the apparent failure to attend to the above-mentioned five elements. A rapid analysis of recent documents issued by the most important exponents of liberal democracy (Group of Seven) shows more declamatory concepts than concrete measures to alleviate inequality, unemployment, and terrorism, and to progress toward genuine free trade (assuming it is an achievable objective). Moving to the Declaration and Plan of Action of the G20, the feeling of distance toward common people's concrete fears prevails. Concern about inequality within countries seems not to be a priority. Placing common people's crucial needs at the forefront is paramount within liberal democratic societies in which the right to dissent is constitutional, and, eventually, can slip toward more robust expressions of protest.

Added to that, there is the "rise of the rest," a group of countries endowed with ancient cultures, consolidating as influential powers. The BRICS (Brazil, Russia, India, China, and South Africa) Goa Declaration embodies its views on the international situation. Many more countries probably can adhere to the BRICS ideology. Due to the absence of the United States and the hints of fragmentation in Europe, the fading of liberal democracy is not going to stop. Nevertheless, liberal institutions, national or international, have, more than ever, a lot to offer. Refugees and displaced people still wish to be relocated in countries that adhere to liberal constitutional democracies.<sup>15</sup>

Reversing the fade of liberal democracy requires much more than specific measures taken, internally and externally, by medium powers. It requires the will and the action of a coalition of countries with different dimensions, under clear leadership, working to recapture the spirit of constitutional democracy, the human rights covenants, and the liberal international order. This will demand domestic modernization (taxation, distribution, social care, humane productivity, upward mobility) and, externally, responsible military power, sound diplomacy, respect for international law and the UN Charter, and a clear understanding of the burden that leadership entails. To put an end to the decline, "many components need to be modernized or supplemented . . . but the international project should be a renovation not a tear down."<sup>16</sup>

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1. I thank the Council on Foreign Relations and Argentine Council for International Relations for the opportunity to briefly comment on what can be done to reverse the fade of liberal democracy. I intend to take up the

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subject with the elements available to a former diplomat. A lot has been said and written on this subject, so I do not intend to be original or creative.

2. Henry Kissinger, *World Order* (New York: Penguin, 2014); Richard Haass, "Where to Go From Here," *Foreign Affairs*, July/August 2017; Richard Haass, *A World in Disarray* (New York: Penguin, 2017).
3. John Ikenberry, "The Rise of China and the Future of the West." *Foreign Affairs*, January/February 2008; Fareed Zakaria, *The Post-American World and the Rise of the Rest* (New York: Penguin, 2009).
4. Ronald Inglehart, "Inequality and Modernization," *Foreign Affairs*, January/February 2016.
5. Inglehart, "Inequality and Modernization."
6. Jerry Muller, "Capitalism and Inequality," *Foreign Affairs*, March/April 2011
7. Luis Moreno Ocampo and Emilio Cardenas, "Agenda International," September/October/November 2004.
8. See also: Fernando Petrella, "Countering Terrorism and Violent Extremism," in the *2015 Council of Councils Annual Conference Panelist Papers*, Council on Foreign Relations, May 2015, [http://cfr.org/content/publications/attachments/Council%20of%20Councils%20Annual%20Conference%202015\\_Panelist%20Papers\\_FINAL.pdf](http://cfr.org/content/publications/attachments/Council%20of%20Councils%20Annual%20Conference%202015_Panelist%20Papers_FINAL.pdf).
9. "G20 Leaders' Declaration: Shaping an Interconnected World," Hamburg, July 2017.
10. Theresa May delivered an impassioned speech at the United Nations, September 20, 2017.
11. Francis Fukuyama, "American Political Decay or Renewal?," *Foreign Affairs*, July/August 2016.
12. Shortly after, Sallustro was assassinated by Montoneros, a Guevarista group in Argentina.
13. Guillermo de la Dehesa, "El Problema del Cambio Climatico," *El Pais*, October 1, 2017; See UN General Debate, 2017.
14. See Fernando Petrella, "Group of Twenty and Global Governance," in the *2015 Council of Councils Fourth Regional Conference Panelist Papers*, Council on Foreign Relations, November 2013, [http://cfr.org/content/publications/attachments/CoC\\_Mexico\\_Panelist\\_Papers.pdf](http://cfr.org/content/publications/attachments/CoC_Mexico_Panelist_Papers.pdf)
15. UNHCR, Global Trends Report, 2016; "Global Migrations Flows," International Organization for Migration, <http://iom.int/world-migration>.
16. Haass, "Where to Go From Here."

# COUNCIL OF COUNCILS

An Initiative of the Council on Foreign Relations



Panelist Paper

## *What Can Be Done to Reverse the Fade of Liberal Democracy*

Council of Councils Tenth Regional Conference

November 5–7, 2017

Argentine Council for International Relations, Buenos Aires, Argentina

**Oliver Stunkel**, Getulio Vargas Foundation

Large parts of the Western Hemisphere and Europe are undergoing a process of profound political uncertainty, marked by low government approval ratings and unprecedented degrees of discontent with democracy in many countries. One consequence is the emergence of outsiders such as U.S. President Donald J. Trump and Brazilian presidential candidates Joao Doria (a businessman and television host) and Jair Bolsonaro (a former military officer). Even moderates in power need to deal with increasingly radicalized political actors and polarized public debates. This trend is more visible in the Americas and Europe, than in other regions of the world, such as Africa and Asia.

The reasons for the crisis of liberal democracy in the West are disputed and varied, though three aspects are worth assessing: rising inequality and a perceived loss of national and cultural identity, the end of the commodity cycle, and the growing influence of authoritarian regimes, especially in China.

In the United States, critical factors in the crisis of liberal democracy seem to be the growing levels of inequality, the sensation that political elites are disconnected, and a sense of loss of identity in an increasingly globalized world. The financial crisis of 2008 in particular has left scars that the country's economic and political elites failed to fully comprehend. A somewhat similar phenomenon is visible in Europe and to some extent in Latin America, where the elites are seen as aloof, self-interested, and incapable.

In Latin America, discontent and political instability are strongly associated with the end of the commodity cycle. Low commodity prices traditionally led to low growth rates across the region and have caused political instability. The economies of Brazil and Venezuela were most affected and shrank 10 percent and 35 percent, respectively, in the last three years. Consequently, the vast majority of Latin American governments grapple with very low approval ratings, as no government can continue the spending largesse that became common during the commodity boom.

Low levels of growth lead to lower public tolerance of corruption, which has contributed to a wave of unprecedented anticorruption protests across Latin America. This situation has made it more difficult for political elites to fight off a new generation of well-trained, popular, and empowered public prosecutors who are investigating corruption in campaign finance and public contracts. The investigation into the Lava Jato scandal in Brazil has spread to many countries in the region, generating additional political uncertainty in, for example, Argentina, Colombia, the Dominican Republic, and Peru.

While governments have embraced the narrative that corruption investigations cause short-term instability but eventually make democracy cleaner and more transparent, there are reasons to worry that broad discontent with politics in general will facilitate the rise of populist outsiders (such as Silvio Berlusconi after the Mani Pulite campaign in Italy). Several populist outsiders have laid out authoritarian approaches and rejected the slow and often frustrating negotiations that are inherent to checks and balances.

The situation is similar in several of the fourteen countries that will have elections in the next two years. Brazil, Chile, Colombia, Costa Rica, Honduras, Mexico, Paraguay, and Venezuela will hold presidential elections in the next eighteen months, and Argentina, Bolivia, El Salvador, Guatemala, Panama, and Uruguay will do so in 2019. Of all the incumbents up for reelection in 2018, only Honduran President Juan Orlando Hernandez (under constitutionally controversial circumstances) and Venezuelan President Nicolas Maduro (in a vote that will likely not be free) can expect to remain in power.

As Latin America faces a potential populist wave, the United States can be seen as a positive example: so far, Congress, courts, and the bureaucracy have been relatively successful at containing Trump's strongman instincts. That has been made easier by the fact that Trump possesses no coherent ideology or, for that matter, interest in governing. He is no match for the far more sophisticated Hugo Chavez, Evo Morales, or Alberto Fujimori, all of whom, from their first day in power, worked to dismantle and erode checks and balances, creating a so-called high-stakes constitution, which concentrates power in the executive.

The shift in power away from the West and the empowerment of authoritarian states that have begun to systematically influence Western democracies are also factors that aggravate the crisis of liberal democracy. Authoritarian states have done so to strengthen their own governments and to weaken the ability of Western states to challenge authoritarianism.

This is becoming clear in the current crisis in Venezuela, where Chinese investments have translated into tremendous political and economic influence. Indeed, no political resolution can be reached in Venezuela today without involving China, which has little interest in letting go of a trusted partner. Over the past few years, China has lent over \$60 billion to Venezuela, most of which is paid back with oil shipments and none of which includes policy conditions. China's pivotal role in Venezuela is only a harbinger of things to come. Chinese trade with Latin America has grown more than twentyfold over the past fifteen years. Chinese President Xi Jinping has announced that Chinese companies will invest a quarter of a trillion dollars in the region over the next ten years, diversifying from traditional industries such as mining, oil, and gas to finance, agriculture, and infrastructure (energy, airports, ports, and roads). This will inevitably enhance not only Beijing's economic influence but also its political clout.

The probability of an effective regional collaboration pressuring the Venezuelan government into starting an earnest dialogue with the opposition is dramatically reduced, as none of the four most influential countries in Venezuela (the United States, China, Cuba, and Russia) is South American. That is partly due to Brazil's internal political and economic crisis, which has limited its capacity to work regionally, creating a leadership vacuum. A broader consequence is that, contrary to the years of the Fernando Henrique Cardoso (1995–2002) and Luiz Inacio Lula da Silva (2003–2010) administrations, there is currently no structured debate among governments about the future of the region to address issues such as lack of physical integration (e.g., infrastructure), trade barriers, how to defend democracy, or how to address China's growing influence.

Most important, however, regional mechanisms created in the 1980s and 1990s through Mercosur or the Organization of American States are largely designed to prevent overt political ruptures. These mechanisms have had a tangible impact over the past two decades, playing a role in avoiding and reversing democratic rifts in places like Paraguay (1996, 1999, and 2012), Venezuela (2002), and Honduras (2009). They are far less effective, however, when those already in power actively undermine democracy. Governments agreed to regional democracy mechanisms as a protection against threats from the barracks, not to restrict their own room for maneuver. This is becoming increasingly obvious in the case of Venezuela, but equally so in Nicaragua and Bolivia, where democracy is under severe threat.

There is no easy response to the difficulties that liberal democracy is facing; however, considering the main reasons above, it is worth pointing in three main directions. First, policymakers should articulate policies to reduce economic inequality, which has worsened considerably since the financial crisis of 2008. Second, Latin American economies need to become less dependent on commodity exports, which are volatile and consequently periodically lead to political crises that hinder democratic consolidation. Third, a broader public debate about how to address the growing influence of authoritarian regimes on democracies is needed. This growth is facilitated by a lack of clear rules in all areas of democratic society, including universities and think tanks (which often accept large donations from nondemocratic regimes), banks and political consulting firms (which help autocrats launder money or polish their image), social media companies (which allow countries such as Russia to influence the public debate in liberal democracies), and governments (which have failed to establish a better screening process for foreign investment from authoritarian regimes in strategic sectors).

# COUNCIL OF COUNCILS

*An Initiative of the Council on Foreign Relations*



## Session Three

### *Combatting Transnational Organized Crime and Corruption*



Panelist Paper

## *Combating Transnational Organized Crime and Corruption*

Council of Councils Tenth Regional Conference

November 5–7, 2017

Argentine Council for International Relations, Buenos Aires, Argentina

**Jessica De Alba Ulloa**, Mexican Council on Foreign Relations

The UN Millennium Project provides an all-purpose list of the types of transnational organized crime (TOC). However, not all types are applicable to all countries or occur at the same rate. Finding common responses will have to happen at a regional level rather than global, because not all responses serve the same purpose everywhere. The will of the nation states is crucial in combating transnational organized crime and corruption.

The following should be prioritized to strengthen the global regime against transnational organized crime:

- **A real rule of law** based on modern, realistic laws needs to be part of the national culture and understood in the context of the Latin phrase *lex regit (la ley rige)* rather than the Spanish equivalent *estado de derecho*, which is more abstract and does not have a direct, empirical impact on the essence of the life and function of a society. As long as there is impunity and laws are bent in accordance with individuals' convenience, it will be difficult, if not impossible, to resolve the common problems of crime and TOC. Each country needs to strengthen its laws and judicial systems. The codification of crimes should also be the same at the regional level so that transnational crimes can be followed and prosecuted in different countries without being obstructed by jurisdictional differences. Latin and Central American governments have been unwilling to unify their criminal laws, making it difficult to follow and punish crime from Tierra de Fuego to, mainly, the United States. Rule of law also means eliminating all official or constitutional perks that provide governmental and political figures immunity from prosecution. Although immunity is intended to protect officials only in the performance of their official duties, not all their acts and actions, it provides officials with the belief, often confirmed in practice, that they are above the law. Countries need the ability to arrest and prosecute anyone, regardless of office or rank.
- **Education, modernization, and professionalization of all police forces**, complemented by salaries that make them part of their country's middle class, need to be a duty of the governments, since they are legally entitled to the use of force to keep order. Governments need to account for this privilege and responsibility.
- **Governmental and political figures should be accountable to civil society for their actions.** Governmental and political figures' privilege has to be eliminated and accountability needs to be enforced. In some countries, along with better or more practical laws, political change through elections can bring progress so that only the will of the people can force change.

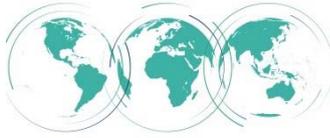
- Government inefficiency is one of the many root causes of corruption. **Review and simplification of laws**, and more flexibility of laws can prevent the practice of offering and demanding “gifts” in exchange for “rapid” or “efficient” services.
- **Finding creative ways to make TOC unprofitable** so that new markets for organized crime do not threaten governments and development is important. In some places, TOC’s convergence with an insurgency or terrorist network is an evolving phenomenon born out of ties of convenience. The world still has not properly adopted a global strategy to counter TOC. TOC is a natural outcome of a global economy and has its own global supply chain management, which often commingles with and depends on regular commercial supply chains. In the face of a politically weak, compartmentalized national approach, transnational criminal networks continue to grow. Crime thrives on easy gains with large profits. Whatever transnational criminals buy, sell, or service should be made unprofitable through legal and proactive law enforcement measures. One major fault today is the lack of effort to confiscate illegal profits and stop money laundering. The legalization of drugs would go a long way to reduce TOC and corruption, though there are some social consequences to be taken into consideration. Only when the TOC supply chains and money flows are disrupted will real change happen. When money is neither abundant nor easy anymore, the participants will be forced to find a different occupation.

Regional and international institutions can increase the capabilities of and collaborative efforts with national governments, particularly in Latin America, to address the root causes of crime in the following ways:

- Most, if not all, governments in Latin America are corrupt. Until civil society is willing to get involved and change the laws and political systems that have fed corruption since the days of Spanish colonization, all efforts will be superficial and pyrrhic.
- International institutions have no real power to enforce any law or behavior, neither from member states nor from individuals. Their support can only be at the micro level, by **implementing programs** to educate young people and supporting efforts to **help people develop themselves and their local economies**. To be helpful, those institutions need to be less bureaucratic and more flexible in using resources in the field.
- Economies, especially in Central America, need to be activated. **Trade agreements** cannot be effective until there is an investment in productive infrastructure, such as the completion of the Central American Railroad (which was poorly managed and abandoned almost one hundred years ago), to ensure development in those economies through commerce.
- National governments should allow **external audits** to confirm their commitment to building strong institutions and fighting corruption. Nations could be expelled from international organizations, such as the International Monetary Fund and United Nations, if they do not comply.
- **States and institutions such as Interpol should work together to enhance the states’ participation and the institutions’ capabilities**, by creating a single criminal database to share information on all criminals with all member states.

Previous initiatives to combat transnational organized crime and corruption have had little value, other than that they looked good on paper. No change will happen unless the root causes of TOC (bad laws, inefficient processes, poorly paid officials, citizens willing to pay for services) are addressed. The initiatives are not wrong; national deficiencies prevent these initiatives from succeeding.

Corruption is the sum of many inefficiencies and deficiencies that promote the need and opportunity to exchange value outside the law. The desire and will to change are the only lessons to be applied. The United States, Canada, and some European States, which while not immune, prosecute those caught in corrupt acts, and the average citizen is neither corrupt nor condones corruption. As long as the average citizen feels empowered to violate simple laws (e.g., running traffic lights or bribing the police), there is no foundation for real change. Generational education from the bottom up holds the only hope for change.



Panelist Paper

## *Combating Transnational Organized Crime and Corruption*

Council of Councils Tenth Regional Conference

November 5–7, 2017

Argentine Council for International Relations, Buenos Aires, Argentina

**Mark Fitzpatrick** and **Srujan Hande**, International Institute for Strategic Studies

As defined by the UN Office on Drugs and Crime, transnational organized crime (TOC) threatens peace and human security and plays a major role in several armed conflicts. For example, the heavy presence of the MS-13 and Barrio 18 gangs in the Northern Triangle of El Salvador, Honduras, and Guatemala is to blame for the region's homicide rate, the highest in the world.<sup>1</sup> While the violence perpetrated by these gangs is typically treated as a domestic matter, it poses a threat to national security. Not only does it take a huge toll on human security and human rights but it also undermines economic, social, cultural, political, and civil development of societies.<sup>2</sup> Such violence goes hand in hand with corruption, undermining governance, rupturing the social contract, and disturbing socioeconomic development. The transnational nature of these crimes is defined not just by the movement and makeup of the gangs but also by the international market for the drugs these gangs supply, the guns they use, and the international cooperation assembled to combat them.<sup>3</sup>

### **Collaborative Strategies to Address the Root Cause of Crime**

The will to confront TOC needs to come from within, but it can be enhanced through collaboration with regional partners. Mexico and its neighbors Honduras and Guatemala have begun to adopt new security policies that integrate civilian and military approaches. New security agencies are being created with a paramilitary orientation, composed mostly of civilians but with military training and discipline. In part, this represents a recognition that police forces lack the training and firepower—or are too corrupt—to tackle powerful transnational criminal groups. It also indicates the drawbacks of relying too heavily on the military. Governments in Mexico and the Northern Triangle have used armed forces several times during the past decade to restore stability and security. However, this has brought allegations of human rights abuses by soldiers, while murder rates have persistently remained high. New agencies and operations have been set up with the aim of applying military-style deterrence and firepower alongside traditional policing tools. The stated aim of most of the new agencies is to reduce abuse claims and civilian casualties while building a permanent deterrence and response force against organized crime. However, the new policies still depend heavily on military approaches, and police reform efforts are progressing slowly.<sup>4</sup>

### **Lessons Learned From Previous Initiatives**

In November 2016, the states in the Northern Triangle created a trilateral force, bringing together a 1,500-person-strong combined force of policy, military, border security, and customs agents. Inspired by the Maya-Chorti task force set up by Guatemala and Honduras, the Northern Triangle effort demonstrates a will to take the fight to the criminals in the region. It is being carried out in conjunction with the Alliance for Prosperity, a foreign aid initiative created jointly by the World Bank, the Organization of American States, and the U.S. government. The mission of this alliance is to counter extortion, kidnapping, money laundering, gang violence, and smuggling. The five tasks are equally important and are given equal prominence. The fundamental aim of this alliance is coordination, allowing for the production of efficient investigations and intelligence sharing.

At the International Institute for Strategic Studies (IISS) conference “The Strategic Implication of Organized Criminal Markets” in Bahrain in 2015, senior government and law enforcement officials, business leaders, representatives from international organizations, and influential experts from a diverse set of countries discussed the dark side of globalization and advances in information technology.<sup>5</sup> The regulation of cross-border activities has become harder, and criminals have benefited from the greater mobility of goods, capital, people, and ideas, as well as from the criminal opportunities presented by the cyber domain. Given the impact of organized criminal activities on state security, governance, development, health, and the environment, TOC is truly a strategic issue. Accordingly, the UN Security Council and development agencies around the world have now included the fight against organized crime among their priorities, making up for lost time—for example, in 2000, when the United Nations missed the connection between TOC and development when adopting the Millennium Development Goals.<sup>6</sup>

As challenges become more complex and hybrid, responses should also become more imaginative, involving public- as well as private-sector actors, local agencies, and international organizations. The IISS conference underscored the proven links between terrorists and criminals, which until some years ago were considered two separate areas of violent activity. There needs to be integration of law enforcement agencies that are often divided neatly into counterterrorism and organized crime. The cyber domain has reinforced a power shift in the relationship between criminals and law enforcement agencies. Whereas organized criminal groups worldwide have been quick to use the internet and other information technologies, many countries lack specialized centers to counter cybercrime. Participatory policing is an important countermeasure. Because cybercrime defies centralized models of law enforcement, agencies should seek cooperation with companies and banks to improve the speed and reach of their efforts.<sup>7</sup>

In recent years, progress has been made in merging security and development approaches to organized crime, with the aim of achieving more sustainable solutions. Despite this, the absence of a global governance structure in the fight against organized crime still prevents a unified and strategic approach. To build greater resilience against TOC, some practitioners pursue high-value targeting to punish and interdict assets and criminals. Other experts note that a focus on suppression or deterrence alone may be impractical or even counterproductive in cases of conflict-affected countries where criminal networks often outdo state resources in terms of arbitration, adjudication, and the provision of security. In such cases, rather than assuming a monolithic criminal-terrorist nexus, it would be necessary to consider managed adaptation of crime and differentiating of criminals. A “good criminal” may be considered someone who poses the least threat to the state, who is kept separate from more destructive groups, and whose access to political capital is eventually severed, leaving limited capacity to corrupt the government.

Fundamentally, policymakers need to recognize the difference between cease-fire politics and policing strategies, and the differences between transactional and predatory criminal activity. Yet there is an inherent danger in assuming that a temporary intersection of interests between states and reformed criminals can guarantee a sustainable alliance of interests; a *Pax Mafiosa* can offer temporary respite but rarely is sustainable.<sup>8</sup>

Although it may be too early to label it a success story, the UN-backed International Commission against Impunity in Guatemala has had notable success in advising the national investigative and justice institutions on the prosecution of high-level corruption. In 2015, it led to the resignation of then President Otto Perez Molina, immediately followed by his arrest on charges of leading a criminal scheme in the country's customs agency. Since then, Honduras has implemented a similar institution, this time backed by the Organization of American States.

Another recent development related to organized crime is the fight against corruption in Brazil. There, TOC has taken a different form, with endemic corruption wasting vast government resources and undermining foreign policy goals. The country's largest construction firm, Odebrecht, has admitted to paying bribes to officials in eleven foreign countries. The good news is that Brazil's sweeping "Car Wash" anticorruption probe, which sent former President Luiz Inacio Lula da Silva to jail and helped impeach former president Dilma Rousseff, is in the hands of a younger generation of prosecutors, judges, and federal police agents independent of political interference. A continuation of these anticorruption efforts can only enhance the country's struggle against poverty and inequality.<sup>9</sup>

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Panelist Paper

## *Transnational Organized Crime and the Illicit Wildlife Trade*

Council of Councils Tenth Regional Conference

November 5–7, 2017

Argentine Council for International Relations, Buenos Aires, Argentina

**Ross Harvey**, South African Institute of International Affairs

Organized crime tends to be associated with arms, narcotics, and human trafficking. Those are indeed the three most prominent forms of international organized crime, and they generate the most revenue. A close fourth, however, and of increasing importance, is the illicit trade in wildlife. It should be a global priority, as it affects a range of important development issues, especially in Africa.

First, it affects biodiversity conservation and wilderness landscape preservation. Elephants, for instance, are a keystone species—their presence is crucial to the survival of entire delicate ecosystems. These ecosystems in turn support tourism, one of the few truly sustainable economic sectors that can fuel Africa's growth in the wake of declining manufacturing jobs due to automation and digitization associated with the Fourth Industrial Revolution.

Second, in many developing countries, transnational organized crime groups infiltrate politics and public service. With highly flexible and well-funded networks, this infiltration corrupts entire sectors from wildlife departments to ports authorities. These levels of corruption are then problematic not only from the perspective of managing ecosystem conservation but also because they constitute a significant barrier to sustainable economic growth. Corruption impedes growth, exacerbates inequality, and worsens poverty. In these contexts, many poor communities turn to illicit activities to make a living.

Third, the growth of transnational organized crime in one area tends to proliferate the growth of organized crime in other sectors, normally through the channel of corruption. In the absence of good governance and resultant alternative economic opportunities, criminal syndicates may be tempted to diversify their activities and ordinary people may find that their only economic prospects are in criminal enterprises. Because syndicates tend to be well organized and have horizontal, flexible network structures, they are also able to interact and trade with each other with a relatively low probability of detection by authorities (if the authorities are not directly complicit). For instance, elephant-poaching and ivory-trafficking syndicates may encourage the simultaneous growth of illicit tanzanite trafficking, or elephant ivory may be traded for arms. The role of ivory in terrorism tends to be overplayed, but its use as a form of currency for procuring other goods is well documented.

In light of these points, transnational organized crime in the illicit wildlife trade should not be treated in isolation from its broader development impacts. It is also not unrelated to the trades in narcotics,

arms, and human beings that tend to arrest the world's attention. Transnational organized crime in elephant-ivory trafficking and rhino-horn smuggling specifically undermines good governance generally and hinders development. Global coordination is necessary to defeat the illicit wildlife trade. The best returns on financial and political capital are likely to be gained in disrupting criminal networks, reducing the demand for illicit wildlife products, and banning their trade entirely. These are the most sensible options, but they are unlikely to work unless all countries collaborate more closely to achieve better outcomes.

### **The Role of Transnational Organized Crime in Elephant-Ivory and Rhino-Horn Trafficking**

Julie Ayling writes that “for the last several thousand years, humans have regarded other sentient and non-sentient species as resources and tradable commodities, a perspective that has often had negative impacts on biodiversity.”<sup>1</sup> She contends that illegal wildlife poaching has the potential to drastically reduce biodiversity by driving species to extinction. Some authors refer to this as the sixth great extinction. Harvesting of natural resources beyond the maximum sustainable yield, poaching, habitat destruction and fragmentation, pollution, and the proliferation of invasive species all portend this ecological crisis. We are in the process of destroying the very source of life.

Illegal wildlife poaching persists despite international resistance and the existence of bodies such as the Convention on Trade in Endangered Species of Wild Fauna and Flora. It is hugely profitable, but profitability alone does not explain its persistence. According to Ayling, “any explanation for the persistence of the illegal wildlife trade requires an understanding of the criminal networks involved.”<sup>2</sup> It was therefore promising that the UN Office for Drugs and Crime released a report in 2016 that recognized wildlife trafficking as “both a specialized area of organized crime and a significant threat to many plant and animal species.”<sup>3</sup> Without disrupting criminal networks, the problem will become intractable.<sup>4</sup> Criminal networks may include organizations, gangs, syndicates, and other collectives. Ayling also notes that “designing effective policies to reduce the illegal wildlife trade requires an understanding of the individuals and groups driving wildlife crime, specific to the geographical area and species.”<sup>5</sup> Two recent reports provide good examples of what is necessary in this respect.

The first is by the Environmental Investigation Agency (EIA). Following its research in Tanzania, the EIA began investigating elephant-ivory smuggling in neighboring Mozambique, and “the investigation revealed a Chinese-led criminal syndicate which for over two decades has been trafficking ivory from Africa to Shuidong, its hometown in southern China. According to this syndicate, it is just one of about ten to twenty similar groups originating from Shuidong.”<sup>6</sup> China implemented a formal domestic ban on its ivory trade on December 31, 2016, which will help to prevent the laundering of illegally imported ivory into a legal domestic market. It closed sixty-seven licensed ivory workshops and retailers by the end of March 2017; the remaining 105 should be closed by the end of the year. However, no notable arrests have been made, which suggests that the criminal syndicates deeply involved in the illicit sale of ivory in China are politically protected. This would also account for the extensive stockpiling of raw ivory that a number of scholars believe is occurring.<sup>7</sup>

According to the EIA, “Located on the coast of Guangdong Province, Shuidong’s emergence as the world’s biggest hub for wholesale ivory trading is rooted in its culture and geography,” and its comparative advantage is rooted in a long history of supplying sea cucumbers from Africa to local markets in China.<sup>8</sup> Its legal sea cucumber business provides a cover for the illicit ivory trade. Over a five-year period—2009 to 2014—Tanzania lost 60 percent of its elephant population and Mozambique lost 53 percent. Due to recently improved law enforcement in the Tanzanian port authorities, the export hubs

of Dar es Salaam and Zanzibar have moved south to Pemba in Mozambique. Elephant tusks are still being harvested out of both the Selous reserve in southern Tanzania and the Niassa reserve in northern Mozambique, however. More than 70 percent of the elephants found dead in the Selous-Niassa ecosystem in 2015 were killed illegally. According to the EIA, “Ivory traffickers rely on the active cooperation or exploitable ignorance of people from a variety of professions—a vital support network which includes corrupt rangers, customs officers, shipping agents, money changers and local fixers.”<sup>9</sup> The EIA report provides a startling amount of detail that helps policymakers understand the details of the illicit ivory trade. Aside from the individual steps that countries such as China, Mozambique, and Tanzania need to take, the EIA report recommends timely coordination between governments and international institutions to share intelligence and enforce legal agreements. One example of this would be the investigation and prosecution of freight agents who facilitate trafficking.

The second report details the anatomy of transnational organized crime in rhino-horn trafficking. Over the last decade, more than six thousand rhinos have been lost. Rademeyer writes, “Driven by seemingly insatiable demand in Southeast Asia and China, rhino horn has become a black market commodity that rivals the value of gold and platinum.”<sup>10</sup> Rademeyer meticulously documents that the criminal networks that traffic rhino horn are ruthlessly efficient, imaginative, and highly adaptive. They are not constrained by bureaucracy and cumbersome laws, or even by international boundaries. More than anything else, disrupting these networks “requires a radical rethink of reactive and fragmented national and international law enforcement strategies and a concerted effort to uplift and include communities living in and around national parks in conservation and law enforcement efforts.”<sup>11</sup>

## **Conclusion**

These two reports demonstrate not only the specific details of transnational organized criminal activity in the illicit ivory and rhino-horn trades but also the severe latent problem of corruption. The networks have become so deeply embedded in the political economy of developing African countries (so-called range states) that new leaders often lack the political capital necessary to root out the kingpins and complicit government officials. This corruption has a deleterious effect not only on biodiversity conservation but also on economies more generally. Corruption invariably exacerbates poverty, and poverty in turn drives poaching in the absence of alternative livelihood options. This is especially true where conservation efforts have historically been associated with colonial endeavors of creating parks that excluded local communities from accessing natural resources. Moreover, because these networks have become deeply embedded and highly proficient, arguments in favor of a legalized trade in either elephant ivory or rhino horn are misplaced. The history of the ivory trade has clearly shown that governments in developing countries are not capable of regulating complex trade regimes. Law enforcement officials have neither the time nor the capital required to distinguish between legal and illegal products, and there is no evidence that consumers of wildlife products desire to consume ethically sourced ivory or rhino horn. A simple, global international and domestic ban on endangered wildlife products would greatly aid international coordination efforts to disrupt organized crime syndicates. However, that in itself, while necessary, would not be sufficient. The final step would be to coordinate efforts to eradicate demand for illicit wildlife products. Achieving this would greatly reduce the negative development impact of organized criminal activity, especially in Africa.

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# COUNCIL OF COUNCILS

*An Initiative of the Council on Foreign Relations*



## Session Five

*Global and Regional Crisis*

*Response: The Case of Venezuela*



Panelist Paper

## *Global and Regional Crisis Response: The Case of Venezuela*

Council of Councils Tenth Regional Conference

November 5–7, 2017

Argentine Council for International Relations, Buenos Aires, Argentina

**Sergio Abreu**, Uruguayan Council for International Relations

Venezuela's situation should be analyzed from three different perspectives:

- **Political:** Venezuela is bound by the Organization of American States Charter, the Ushuaia Treaty, and the Union of South American Nations (UNASUR) Treaty, among others. The democratic clauses in these treaties are clear, and are not being honored. The authoritarian populism goes against the peaceful transfer of power and separation of powers. The first sanction against a member state that violates the treaty would be its suspension. UNASUR provides for serious economic sanctions and the suspension of the country's status as member of an international organization.
- **Economic:** Venezuela's economy is technically in default. It depends exclusively on Russia's support, which refinanced a \$17 billion loan and purchased oil, paying for it in advance. The price of oil is a critical economic factor, however, in maintaining Venezuela's relationship with its allies. To ensure their support, Venezuela delivers hundreds of thousands of liters of oil daily to Cuba and other Caribbean countries.
- **Strategic:** Venezuela is the strategic wedge in the Southern Hemisphere for China, Cuba, Iran, and Russia. Its connection with Bolivia increases the polarization between its twenty-first-century socialism and the United States, providing a symbol of anti-imperialist struggle and an excuse for irrational nationalism. Nonetheless, the logistic support and administration of the concentration of power basically stems from Cuba.

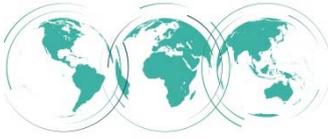
### **Options**

Sanctions set forth in treaties should be applied. However, there are not enough country votes to enact sanctions, except in Mercosur, from which Venezuela was suspended.

National governments and international institutions could apply economic and other types of sanctions, as is the case with the European Union. Measures should be taken to avoid people from believing that they will be adversely affected by sanctions against the government. The fight against drug trafficking and narco-states should include Venezuela. International criminal law should be applied to Nicolas Maduro's government.

Unilateral military intervention is unacceptable and useless. All actions should be in accordance with international law and not confuse citizens with government. In that regard, President Donald J. Trump's statements are annoying and provide an excuse for Venezuela to continue its anti-imperialist

rhetoric. As suggested by Colombia's president, all support should be aimed at strengthening Venezuela's political parties and pressuring the government to hold elections. A divided opposition is the engine that drives imperialism.



Panelist Paper

## *Global and Regional Crisis Response: The Case of Venezuela*

Council of Councils Tenth Regional Conference

November 5–7, 2017

Argentine Council for International Relations, Buenos Aires, Argentina

**Haibin Niu**, Shanghai Institutes for International Studies

### **The Nature of the Venezuelan Situation**

With U.S. President Donald J. Trump raising the possibility of a military option in Venezuela in August 2017, the current situation in Venezuela should be examined. The Trump administration has enacted financial sanctions against Venezuelan senior officials for abusing human rights and undermining democratic processes. U.S. Ambassador to the United Nations Nikki Haley alleged that the situation in Venezuela was on the verge of a humanitarian crisis when she tried to add the issue to the UN Security Council agenda. These actions show that the United States treats the nature of the Venezuelan crisis as mainly political even though there are several social and economic issues in play. Besides the economic shortages caused by falling oil prices, high welfare spending, and mismanagement, international concern and action has been directed at addressing the denial of political rights to Venezuela's opposition, as demonstrated by Venezuela's suspension from Mercosur, the Lima Group's Declaration, and the postponement of the regional summit with the European Union.

Some facts need to be considered when discussing the multiple crises in Venezuela. First, the government has not defaulted on its debt even though there were indications that it might. This shows that the oil revenue can help the regime weather financial hardship. Second, the lack of consensus within the Organization of American States (OAS) on whether Nicolas Maduro violated the Inter-American Democratic Charter and the result of recent regional elections in Venezuela shows that the Maduro administration still has meaningful regional and domestic support. Third, Maduro's diplomatic efforts have been relatively well received by members of the Organization of Petroleum Exporting Countries as they face strong competition from U.S. oil exports. Fourth, the domestic situation is still in the hands of the consolidated Maduro administration. It created the National Constituent Assembly, ended the violent protests, won the regional election in many states, and maintained the loyalty of the military. Finally, the uncompromising postures of both the Maduro administration and the opposition indicate that a resolution to the crises could have to wait for the next general election.

### **The International Response to the Venezuelan Crisis**

Regional and international efforts to restore the power of the national assembly, release jailed opposition leaders, and adopt economic measures have failed. OAS cannot build a unified position on Venezuela because Venezuela has a subregional influence via its Bolivarian Alliance for the Americas and oil diplomacy with the Caribbean nations. Venezuela's major economic partners are the United States, China, and Cuba, which makes the economic pressure from Mercosur and the Lima group less relevant.

The United States also hesitates to impose strong economic sanctions against Venezuela because the U.S. refinery sector has strong ties with the country. In addition, Venezuela has built a comprehensive strategic partnership with China since the early 2000s. Colombia cannot take an aggressive policy stance against the Maduro administration because it has many Venezuelan immigrants and the two countries share a long and porous border. Russia also reinforced its relationship with Venezuela, which has helped Maduro consolidate his domestic power. This relative economic independence offers Maduro the space to resist external political pressures.

The changing regional context also will not facilitate domestic reconciliation in Venezuela. In the eyes of the Maduro administration, Argentina and Brazil are becoming unfriendly under the new leadership of Presidents Mauricio Macri and Michel Miguel Elias Temer Lulia, respectively. This reduces the legitimacy of the Union of South American Nations' mediation efforts in Venezuela. In this context, the less influential Dominican President Danilo Medina has tried to play a mediating role. The region generally expressed its support of the Barack Obama administration's declaration that the Monroe Doctrine was over and that he valued the region's peace and autonomy. Latin American countries are still watching the Trump administration's policies toward the region and oppose any kind of U.S. measures considered as interventionist. The parallel court installed by the Venezuelan opposition at OAS did not generate support from ambassadors across the region regardless of their attitudes toward the Maduro administration. The Venezuelan opposition's strategy to oust Maduro from office was mainly focused on domestic protests and building an alliance with the United States and Europe rather than focusing on the next general election. The opposition's choice also reflected a dilemma for regional right-wing politicians who have less chance of winning general elections by emphasizing the role of the market over welfare. Therefore, judicial and legislative channels were used to achieve a change in administrative leadership, which increased regional and domestic uncertainty. The opposition and the right-wing politicians need to have more serious dialogue and reach a rapprochement in order to better prepare for the 2018 general elections.

### **Evaluating China's Relationship With Venezuela**

China's relationship with Venezuela is an indicator of the deepening relations between China and Latin America in the past two decades. Venezuela represents the region's left politicians' new world vision with an external priority given to the global south. Former President Hugo Chavez made efforts to establish a strategic partnership and strong commercial ties with China. Despite the ups and downs of the commercial relationship, both governments maintain their commitment to the strategic relationship. China also appreciates Venezuela's support of China's position in the South China Sea, China's seventieth anniversary military parade commemorating the end of World War II, the China-CELAC Forum, Asian Infrastructure Investment Bank, and the Belt and Road Initiative, among others.

The "loans for oil" program developed by Chinese and Venezuelan governments deepen the bilateral economic ties. China benefits from the supply of oil and investment opportunities in Venezuela, even as Chinese companies have suffered from the recent years of recession in Venezuela. China made efforts to help Venezuela overcome its economic crisis by rolling over the Venezuelan debt. The deep political and economic crises that left millions facing shortages of basic goods were reported by Chinese media and caused concern for the security of Chinese investment and loans in Venezuela. To some extent, Venezuela's attractiveness to Chinese investors was downgraded in recent years due to its worsening business environment. China faces the challenge of protecting its overseas interests in multiple ongoing crises in countries such as Venezuela.

Apart from the rollover of Venezuelan debt, China also supports the Maduro administration's efforts to diversify its economic industrial structure and other economic measures such as energy price changes. To some extent, the China-Venezuela economic relationship is representative of the structure of trade between China and Latin America. The commodity-intensive countries are economically vulnerable since the end of the period of high-priced raw materials. For China, maintaining complementary economic ties with Venezuela based on the demand and supply of oil while helping Venezuela update its economic structure is a big challenge. China's attitude toward Venezuela also goes beyond economic interests in that it maintains its commitment to the comprehensive strategic partnership.

In a recent report to the U.S. Senate Armed Services Committee, Admiral Kurt W. Tidd called China's relationship with Latin American countries a threat to long-term U.S. objectives and interests. This observation shows that the U.S. concerns of strategic competition with China are not limited to East Asia. China has generally been cautious in developing security cooperation with countries characterized as anti-American. The increasing security and high-tech cooperation through sales of arms and satellites is in the range of comprehensive strategic partnership but does not mean that China supports the anti-American agenda of some Latin American countries, including Venezuela.

# COUNCIL OF COUNCILS

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Panelist Paper

## *Without Diplomacy, Sanctions on Venezuela Will Fail*

Council of Councils Tenth Regional Conference

November 5–7, 2017

Argentine Council for International Relations, Buenos Aires, Argentina

**Shannon O’Neil**, Council on Foreign Relations

Despite condemnation from forty countries and even the Pope, Venezuela’s ruling party installed its new assembly in August 2017. Choosing as its head former Foreign Minister Delcy Rodríguez, a loyal follower of President Nicolás Maduro, the assembly focused on efforts to stifle any dissent, beginning deliberations to undermine the opposition-controlled legislature and restructure the government.

The government swiftly moved to consolidate its broader authoritarian grip, firing state workers who did not vote, punishing the last remaining independent media outlets, ousting the outspoken attorney general, Luisa Ortega, and arresting many opposition figures.

As Venezuela descends into full authoritarianism, closing down any space for the political opposition and threatening basic freedom of expression and human rights, the United States should be pressed to do more.

In the lead-up to Venezuela’s illegitimate election, the United States promised “strong and swift actions against the architects of authoritarianism.” Even with President Donald J. Trump’s August 11 announcement that he would consider military intervention, his initial reaction has been surprisingly mild. Its sole move was to make Maduro an international persona non grata, joining the likes of Zimbabwe’s Robert Mugabe, North Korea’s Kim Jong-un, and Syria’s Bashar al-Assad.

Maduro responded with ridicule and undoubtedly relief. He took to Venezuela’s airwaves to jeer President Trump to “bring on more sanctions” as in his earlier “I don’t listen to orders from the empire, not now or ever.” Meanwhile PDVSA, the state oil company, quietly continued to ship some 700,000 barrels of oil a day to U.S. refineries scattered in Texas, Louisiana, and Mississippi, netting Maduro and his ruling cabal over \$150 million in hard currency in the beginning of August.

Indeed, the United States has to take stronger actions than the variety of sanctions that it has already imposed against Venezuela. It can expand the current list of some two dozen targeted individuals to include the members of the new Constituent Assembly and others, freezing their assets, banning them from the United States, and forbidding them from doing business with U.S. citizens. This would hamper the lush lifestyle of the elite—curtailing surfing on Australia’s Bondi Beach, studies at the Sorbonne, and the lavish vacations Venezuela’s so-called Bolivarian princelings and princesslings reveal in their online selfies.

But expanding individual sanctions will do little to change anything on the ground.

The United States could next ban the sale of the lighter U.S. crude oil and diluents Venezuela needs to get its heavier crude out of the ground, processed, and suitable for export. This would temporarily disrupt production as the South American nation looks for other sources.

A bigger step would be to disrupt the flow of money and oil between Venezuela and the United States. The United States could refuse to pay PDVSA directly for oil shipped to U.S. refineries, instead setting up an account, along the lines of the UN Iraqi Oil-for-Food program, that would let the government only use the money to buy food and medicines. Maduro would be unlikely to accept these terms, searching for other markets for its products—India, China, and Russia the most likely recipients. On the financial side, the United States could ban the nation from accessing the U.S. banking system, limiting its ability to trade and to service its debt. Or the United States could impose a full embargo on Venezuela's oil and petroleum products.

These options would devastate Venezuela's remaining economy, limiting already scarce basic goods. An oil or financial ban would likely lead the country into default on its over \$100 billion dollars in foreign debt. But they are unlikely to revive Venezuela's democracy. Over the last seventy years the United States has sanctioned over two dozen nations—Russia, North Korea, Cuba, Iran, Syria, Burma, and the Ivory Coast among them. None of those sanctions have led to swift political change.

Iran, the most recent and relatively successful use of sanctions against an oil-rich nation, shows the decisive limits. Rolled out over nearly a decade, first under President George W. Bush and then expanded under President Barack Obama, these restrictions united the UN Security Council and countries East to West across ideological lines to exclude the Middle Eastern nation from oil, financial, and commercial markets. Hobbled by diplomatic isolation and economic recession, Iran came to the negotiating table, ultimately agreeing to limit its nuclear program. But the Ayatollah remains fully in power.

Worse, the United States has yet to invest in diplomacy. The depleted state department's absence was keenly felt in June, when Secretary of State Rex Tillerson failed to show up at the regional Organization of American States meeting, letting a vote to condemn Maduro's actions fail despite strong support from Mexico, Peru, Argentina, Colombia, and others. Without U.S. leadership and leverage, many Caribbean islands, including the Bahamas, Barbados, Jamaica, and Guyana, remained on the fence, denying the multilateral organization necessary for a two-thirds majority.

The lack of diplomacy means the United States has yet to convert the rhetorical condemnations of European and Latin American countries into concrete actions that would support and bolster the reach of U.S. steps. And it augurs poorly for any active UN role, as Russia and China are sure to oppose punitive measures, but could, with pressure, potentially be convinced of the need for humanitarian relief.

As officials debate sanctioning Venezuela, Cuba remains the most likely and cautionary path. As the embargo against the island enters its fifty-seventh year, a Castro remains president, the government authoritarian, and two generations have grown up believing the United States is the villain behind their economic and political distress. Similar restrictions would grant Venezuela the same narrative, providing a scapegoat for their homegrown catastrophe.

Cuba's shadow hangs over the Western Hemisphere in broader ways, dividing the rest of the region from the United States. An economy-wide hit on Venezuela would likely quiet the strong anti-Maduro stances taken by Latin America's leaders, Venezuela's sins paling in comparison to the perceived historical ones of the United States, making it difficult to build the necessary multinational support to make such sanctions effective.

On principle the United States should stand up to the Venezuelan regime. Rallying the world to defend democracy matters, as does humanitarian relief for Venezuelans' immense suffering. But true progress will require heavy diplomacy, building a broad coalition of nations to deny Venezuela's authoritarian leaders admittance to the global community and to support its beleaguered people. Sanctions are one tool. But they do not work in a diplomatic vacuum. And do not expect them to bring regime change.

*This paper appeared as an article on CNN.com: "Venezuelan Sanctions Without Diplomacy Will Fail," CNN, August 13, 2017, <http://cnn.com/2017/08/13/opinions/venezuelan-sanction-failure-opinion-oneil/index.html>*