Dear reader,

Welcome to the inaugural issue of Politik at UNSW. With the launch of this issue comes the launch of a new endeavour and a host of challenging student ideas.

Over the semesters to come, Politik will be a canvas for students and academics to paint a multi-dimensional picture of the world as they see it. International affairs is the nexus at which key disciplines overlap, and in this spirit, Politik will explore not only the issues facing the major regions of the world, but also the contemporary challenges posed to global science, the environment, health, business and economics.

It is 2014 and we have firmly set our foot in the door of the new millennium. The global landscape has significantly changed and today we can see a range of new challenges arising from our struggle to reconcile the past and the present, the Old World and the New World. In the following pages, we will explore some of these key issues.

To begin, the international status quo has much changed and the days of an unchecked Western world order are over. Much has been made of the rise of China, but truly discerning China’s motives, as well as the future reach of the United States, is proving difficult.

The global spread of democracy since the 20th century has been far-reaching but troubled. In the non-Western sphere, democracy frequently battles with corruption in the electoral process, as in Indonesia, and it struggles with drastically different local political cultures in nascent states. In the Western sphere, fair representation and process efficiency remain ongoing democratic challenges for nations and supranational bodies such as the European Union.

The question of the environment grows ever more pressing and is brewing a new threat of resource conflicts and energy scarcity, as in Africa. As a result, the imperative to forge a new path in clean and sustainable energy sources is stronger than ever, and perhaps fusion energy provides an answer.

The new world sees traditional problems take on non-traditional faces. In the case of disease, conflict and migration, the social and public health dimensions of these issues are worth critically examining, from HIV/AIDS to internally displaced persons.

Finally, the fast-paced business world is today evolving to embrace new forms of media and communication, but is still reeling from the first financial crisis of the new millennium. Analysing the causes of financial fragility is crucial in planning the way forward.

In this issue, we hope to explore some of the knowns, unknowns, certainties and risks that the international community faces as we settle into a new era. We hope that you will find the following articles by students from all over the university both informative and insightful.

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Will China dominate the 21st Century?

Clement Chen

Napoleon Bonaparte once warned: “Let China sleep for when she awakes, she will shake the world.” After the emergence of Deng Xiaoping as the ‘paramount leader’ in 1978 and the subsequent rapid economic growth of China, Napoleon’s prophetic warning has come to dominate international discourse. The emergence of China as the primary challenger to a largely US-dominated world has led many to revisit Napoleon’s warning and ask, “will China dominate the 21st century?” In order to answer this critical question, the following underlying questions will be examined:

- Is China willing to dominate the 21st Century?
- Will China’s return to pre-eminence continue or will it collapse?

China’s rise must be considered in the context of China’s rich history as the world’s longest continuous civilisation. For the majority of history, China was the largest and most advanced economy in the world. From the onset of global trade, China served as the world’s ‘silver sink’, whereby global trade functioned to produce and transport silver to purchase Chinese goods. This continued until the catastrophic Opium Wars of the mid-19th century and the beginning of the ‘Century of Humiliation’, which featured revolution, civil war, warlordism, foreign intervention and the rise of the Communist Party.

The years of turmoil were finally brought to an end with the ascendancy of Deng Xiaoping. Deng undertook the policy of gaige kaifang (reform and opening up), which saw China’s economy expand to become the second largest economy in the world. The rapid growth in Chinese economic power and its increase in political clout have led to much debate over the ‘rise of China’. However, in the context of history, the ‘rise of China’ is not that of a new power in ascendance, but it is, as Napoleon predicted, ‘the return of China’ to its former pre-eminent role.

Is China willing to dominate the 21st Century?

As a result of the ‘China threat thesis’ there is a view that China seeks to displace US hegemony and install a China-led order. Although this thesis is a valid argument and is reflective of the changing geopolitical landscape, the concept that China’s return is a direct and concerted threat to the West is an example of anachronistic Cold War thinking and indicative of a West that feels under siege.

‘The Beijing Consensus’ and the regime’s adherence to political self-determination serves as the guiding principle behind China’s foreign policy, which appears to suggest that China will not seek to dominate the world. This also comes of China’s history and its fundamental ties to Confucianism, which seeks harmony and order above all else. This interest in preserving peace and order is reflected in China’s presence at negotiations over the North Korean and Iranian nuclear programs, for example. China does not seek to dominate the world from the top. Rather, it wishes to become a key stakeholder in a “horizontal world order” where China has reached a state of parity with the US.

Ultimately, there is little chance that China would seek to unilaterally dominate the 21st Century; in fact it intends to integrate itself within and preserve a more equal world order. However this is all predicated on China’s continual rise, and the assumption that it will not suffer from a critical collapse, something many Western observers have predicted. This leads us to the question:

Will China’s return to pre-eminence continue or will it collapse?

China’s economic development has been uneven and until recently has been mostly confined to the eastern and southern coastlines, leading to a growing gap between the interior provinces and the developed
coastal provinces. Susan Shirk argues that this gap will be a major source of unrest and has turned China into a “fragile superpower”.9 However, throughout China’s history there has always been a great difference between its various regions, as China has always used its vastness to its advantage, allocating resources and talent to particular areas first.10 In his “China’s 1+1>2” thesis, Zhang Weiwei argues that this is in fact China’s strength, as China can now focus all of its resources in developing individual provinces (which are on average the size of an European state) in a piecemeal fashion rather than attempt to develop a continental entity as a singular unit. Such a development model would not be sustainable for a conventional nation-state. However, China is a civilisation-state with an inherent adaptability that allows it to maintain a measure of unity between diverse regions and peoples, although often critically tested. This policy was captured by Deng Xiaoping with his words: “Guangdong should take the lead in surpassing the ‘four little dragons’” and “Shanghai is our trump card”.11

A common argument is that the current regime cannot be legitimate if it does not embrace democracy. However, the Chinese state’s legitimacy lies within its Confucian tradition. The Chinese word for state, guojia, is literally ‘nation-family’ and as such, the legitimacy of the central government lies within its position as the head of this family.12 The role of the Chinese state has traditionally hinged upon two Confucian concepts: minxin xiangbei (winning the people’s hearts and minds) and xuanxian renneng (selecting talents based on meritocracy).13 If the government lost the ‘people’s hearts and minds’ then it would lose the ‘Mandate of Heaven’ and all legitimacy. Moreover, China’s historical emphasis on meritocratic governance has continued on to today, with leaders who may not have been elected to power, but leaders who have earned their positions through years of work and education.14 As such, the regime’s Confucian influences and its focus on meritocratic governance for the people has ensured it a great deal of legitimacy.

For much of history, China has been the center of the global economy and the hegemon within a Sinosphere. However, due to a litany of reasons, China lost this position to the West. This downfall has reversed, and China has seen a rapid return to its former role. Napoleon’s warning appears to have come true; China will sooner, rather than later, become the dominant economic power. Will China use its role and power to dominate the 21st Century and displace the United States as the global hegemon? This scenario seems unlikely, due to China’s own Confucian traditions of preserving harmony and order, and the rise of multilateralism. The argument that China will collapse before it can resume its superpower status on par with the US appears short-sighted and neglects the inherent adaptability of the Chinese state. Ultimately, China will continue to rise, and all other states will have to accept a multilateral world in which China is one of the key stakeholders.

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The Personalisation of Politics: Issues in Indonesia’s Electoral System

Hannah Figueroa-Crisostomo

Amongst the commentary and debates regarding Indonesia’s legislative elections held in April this year and its presidential elections to be held in July, there have been numerous reports on the ongoing deficiencies of party candidate recruitment and the weak nature of the political party system. In particular, there is a broad consensus that these weaknesses are linked to the enduring features of Indonesia’s socio-political sphere: corruption, nepotism and clientelism. In describing the current patterns of candidate recruitment and party institutionalisation in Indonesia, I will explore why political parties continue to draw ire in Indonesia’s democratic process. I will also draw attention to the relatively undocumented but increasing stake the Indonesian electorate have in determining political power and party transformations today, as well as key reforms that are underway.

The “personalisation” of the Indonesian electoral system: roots and causes

Indonesia is the world’s third-largest democracy and a leading example of a successful transition from an authoritarian, single-party regime to a democratic multi-ethnic state resting on a model of regional autonomy. However, the country’s political system continues to be mired by corruption, nepotism and clientelism. In 2013, Indonesia was ranked 114th worst out of 177 countries for institutional corruption. It is estimated that half of local government officials across the archipelago are currently under investigation for corruption, while senior police officials, party representatives and Constitutional Court judges have also been previously implicated in corruption scandals.

Despite the consistent emergence of corruption cases and the subsequent strained relationship between parties and the electorate, electoral democracy is nevertheless overwhelmingly supported in Indonesia. This support is facilitated by Indonesia’s electoral laws, which create a system that does not favour the rule of a majority party (or coalition of parties) and which does not encourage the Indonesian electorate to vote based upon political party platforms or ideology.

Under current electoral laws, the president, provincial governors, mayors and district heads are directly elected in separate polls after the legislative candidates have been elected. In this way, a new national parliament is formed. In the legislative elections, a political party (or a coalition of parties) must secure a minimum of 25% of the popular vote or 20% of the seats to be able to nominate a candidate to contest the subsequent presidential elections. As a consequence, constituencies rely on the personal attributes and histories of candidates to decide who to install and uninstall from office, while Indonesian parties establish broad coalitions in order to gain political power and to form government.

Is the personalisation of Indonesian politics a bad thing?

Many argue that the ‘personality-based’ voting behaviour of the Indonesian electorate is one of the underlying reasons that money politics persists in election
the voting public’s concern with the individual, rather than party ideology or platform, is widely acknowledged to have caused the expansion of Indonesia’s political landscape to include caleg cantik (or ‘pretty candidates’, though the term applies generally to singers, actors and TV personalities) and dynastic members.

More crucially, the voting public’s concern with the individual, rather than party ideology or platform, is widely acknowledged to have caused the expansion of Indonesia’s political landscape to include caleg cantik (or ‘pretty candidates’, though the term applies generally to singers, actors and TV personalities) and dynastic members. Among the candidates who ran at this year’s general legislative elections, 10 were current Cabinet Ministers, 51 were caleg cantik, 15 were relatives of President Susilo Bambang Yudhoyono and a few were wives of the Minister of Religious Affairs and the Minister of Cooperative and Small Medium Enterprises.

As Indonesia’s three previous free elections demonstrate, parties endorse individuals with existing public profiles to finance party campaigns and to secure votes, particularly since potential candidates are required to contribute substantial funds to the party if they wish to run for office. As such, many elected politicians are ill-informed of, or neglect to observe, regulations regarding how government operates, and the functions and proper roles of legislators.

But while Indonesia’s politico-social elite were overrepresented in this year’s nominee list, there were also numerous candidates with less glamorous backgrounds, or candidates who were former celebrities and who have since contributed to the policy-making process and helped improve the country. While some analysts argue that celebrities, TV personalities and members of political dynasties have a greater chance of being elected owing to their high level of appeal and visibility in the media, this underestimates the extent to which the Indonesian people critically evaluate and respond to their electoral process.

The Indonesian electorate is playing an increasing role of civic engagement in political party transformations and, more broadly speaking, in the process of Indonesia’s democratic consolidation. This is due largely to the work of the traditional media and the ubiquity of the internet and social media, which have transformed the way in which power is negotiated, aggregated, shaped and exercised - ‘politics’ in its most prosaic of terms.

Exposing and informing the public of political corruption has become the modus operandi of the Indonesian mainstream media, with corruption scandals making daily headlines. A relentlessly information-saturated environment feeding into the public domain, however, can challenge the capacity of both the body politic and the state to understand and respond in considered ways; the media’s constant demands for accountability, while crucial in ensuring political accountability, may take precedence over the media discharging its other significant role, that of generating substantive issue-oriented political debate and, more crucially, of educating the public on the political and electoral system. The lack of sufficient education among many Indonesian politicians about government process - whether legitimately elected or otherwise - could be seen to reflect a gap in the public consciousness of Indonesia’s political system and its intricacies.

Reforms to address systemic and structural deficiencies of the electoral system

Deficiencies in candidate recruitment and party institutionalisation in Indonesia have been met with numerous proposals and strategies for reform. Joko Widodo, the popular governor of Jakarta and favourite to become President, gave his support to making it mandatory for political parties to select candidates democratically, either through convention or internal election, rather than by appointment.

At the time of writing, the Indonesian government has proposed that an anti-dynastic clause be inserted into the new Regional Election Bill to bar candidates who are relatives of incumbents from contesting so as
to prevent the emergence of local political dynasties. They can take part only in the next election to prevent consecutive succession. One drawback, however, is that such an anti-dynasty clause does not stop incumbents from appointing a proxy who would do their bidding once elected. The clause also contravenes the principle of equal recognition of the right to stand in election.

In addition, the Constitutional Court recently ruled that the electoral rules, with respect to the thresholds to be met by parties to nominate presidential candidates, and the requirement for voters to first elect the parliament and then a president, are both unconstitutional. However the subsequent electoral changes will not come into force until the 2019 election.

Lastly, in the way of reform, political parties and candidates have worked with journalists in an effort to stem money politics and produce free and fair elections. As a result of their collaboration, a series of investigative journalism pieces exposing corrupt practices in the recent general elections has been produced. Civil society organisations and media organisations have cooperated to create and implement innovative strategies to monitor April’s legislative elections, and will presumably do so again in the presidential elections. Indonesian civil society has begun to focus on strengthening the connections between voters, candidates, and information sharing. As Indonesians are some of the most active social media users in the world, civil society organisations have designed apps and websites to provide a variety of channels for newly-elected politicians to reach out to their constituencies.

Indonesia is a successful but flawed democracy. While the electoral process has worked well, the quality of democratic governance is less encouraging. Institutional and systemic factors such as the arbitrary enforcement of electoral laws are largely responsible for making the democratic space of Indonesia static. However, such conditions have certainly not made the country’s voting population disengaged in the political process; Indonesia has both a strong civil society and a free and diversified media with an enthusiasm to realise transparent, open elections and ultimately achieve transparent and corruption-free governance.

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3. According to the Asia Foundation’s 2013 “Survey of Voter Knowledge, Attitude, and Practices”, 98 percent and 86 percent of voters believed presidential and legislative elections, respectively, were important, with a significant portion of them considering these elections to be “very important.”; see in S. Hamid, ‘Indonesia’s Election Activists Fight to End Money Politics’, The Asia Foundation, 22 January 2014, http://asiafoundation.org/in-asia/2014/01/22/indonesias-election-activists-fight-to-end-money-politics/ (accessed 14 April 2014).
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The European Union (EU) is, in many respects, an anomaly. Never before have we witnessed such a voluntary pooling of national sovereignty in the interests of collective policy and decision-making. Never before have we seen the elimination of trade barriers or the virtual disappearance of internal borders as in the EU. From its rather humble origins as a six-member trade regime (in the guise of the European Coal and Steel Community (ECSC) and the European Economic Community (EEC)), the EU has undertaken several expansion projects in reaching its current form of 28 member states. However, the diversity of EU member states requires maintaining a careful diplomatic equilibrium in determining the influence wielded by each country, dominant powers and smaller states alike. November 2014 will see the implementation of a new voting regime in the EU’s Council of Ministers, which will redistribute voting allocations across all member states. This article will examine the impact this reform will have on the power of small states in the EU.

How do we define a ‘small state’? In its simplest form, the term can be used to refer to member states “that have less than average voting power in the Council of Ministers”.\(^1\) Under the current construction of the Council, the average number of votes is 12.54.\(^2\) This suggests that 20 of the present 28 EU members are ‘small states’.

Of the six founding members (Belgium, France, West Germany, Italy, Luxembourg and the Netherlands), one third (or arguably, half, if we also include the Netherlands) were
smaller states must stretch their resources in order to develop a strong influence to counterbalance the policy machines of their larger neighbours.

‘s small states’. According to Paul Magnette and Kalypso Nicolaidis, this meant that smaller states benefited “disproportionately from the pooling of sovereignty”. With this in mind, the enlargements of 1995, 2004, 2007 and 2013 have largely resulted in the incorporation of many other small states into the EU framework. A number of these states wield considerable influence within the institution, which is hardly surprising given the nature of the EU’s development.

Indeed, despite its tiny population (approximately 493,500 in 2011), Luxembourg is surprisingly influential. Sasha Baillie argues that Luxembourg’s status as a founding member of the precursors to the EU is fundamental to its contemporary position as an influential regional actor, in spite of its ‘small’ size. This is helped by the location of key EU institutions (such as the Court of Justice) in the heart of the tiny nation state. Being so closely tied to the foundation of the EU, Luxembourg’s presidencies of the Council have witnessed some of the most fruitful periods of integration. Certainly, Luxembourg oversaw the enactment of the Single European Act in 1986, initiated the Intergovernmental Conference leading to the Maastricht Treaty (1992), and launched negotiations that resulted in the accession of 12 new member states in 2004 and 2007. However, notwithstanding Luxembourg’s evident proactivity in EU affairs, it must also be borne in mind that the nature of the ‘rotating’ presidency of the Council means policy-making is the responsibility of a troika of decision-makers, not just the incumbent.

Nevertheless, small states face inherent difficulties if they hope to exercise a strong influence in the EU. For instance, while the French foreign office employs over 9,400 people, its counterpart in Luxembourg sustains a mere 200. It follows that smaller states must stretch their resources in order to develop a strong influence to counterbalance the policy machines of their larger neighbours.

The reforms envisioned by the Lisbon Treaty (signed 1 December 2007 and entered into force 1 December 2009) have been progressively implemented on a step-by-step basis. Later this year, the distribution of power amongst member states will subtly change. Although the reforms will impact the ability of small states to wield a stronger influence within the EU, it does not follow that they will lose all importance under the new regime. The most relevant reform here relates to the allocation of votes within the Council of Ministers.

From November 1, the Council of Ministers will adopt a system of ‘double-majority’ voting to reach its decisions. This relies on a motion winning the support of a majority (55%) of member states, representing 65% of the EU’s total population. In practice, this will reduce the voting power of every small state in the Council. A corollary of this is that it will become harder
for smaller states to build minority coalitions to alter the course of a decision. However the Treaty envisages certain safeguards that are specifically designed to protect smaller states. For instance, a blocking minority must be supported by at least four member states.\(^\text{10}\) As Fiona Hayes-Renshaw points out, this ensures that two or three larger member states cannot use their voting power to block proposals out of hand.\(^\text{11}\)

While the reforms mean that the voting power of small states in the Council will be somewhat reduced, the proposed changes in the European Parliament (EP) will be slightly less significant. Indeed, the Treaty sets a minimum threshold of six seats in the EP per member state, with a maximum allocation of 96.\(^\text{12}\) As such no small state will lose representation in the Parliament. Additionally, the EP’s competences will be expanded under the reforms, which will further preserve the existing scope for small states to influence EU policy.\(^\text{13}\)

What, then, do the Lisbon reforms mean for the future of small states in the EU framework? Firstly, they do not signal their demise. The reforms have been designed to render the EU more democratic by apportioning voting power relative to a state’s domestic population. The fact that Germany will hold 96 seats in the EP is a simple reflection of its demographic reality – the country constitutes some 82 million European citizens.\(^\text{14}\) Likewise, Malta’s 6 seats in the EP reflect its significantly smaller population of 413,630.\(^\text{15}\)

The Lisbon reforms are not designed to obliterate the power of small states to contribute to the development of EU law and policy. It would be melodramatic and inaccurate to suggest the impending changes signal an end to their influence. Certainly, the reforms will reduce the voting power of smaller member states. Yet this represents a broader trend towards supranationalism in EU affairs. The EU is seeking to better represent the interests of its citizens, and in doing so it attempts to distance itself further from the traditional model of sovereign nation states.

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Lessons in state-building to take from Europe

Uzma Sherieff

The global landscape today is peppered with examples of how internal conflict can devastate a nation’s stability and development progress. In recent decades, the international community has opted to pick up the pieces, and ‘state-building’ has risen to the forefront of international development policy. From Afghanistan to Bosnia to Haiti, state-building sees developed nations pledge themselves to foster institutions and strengthen the capacity of fragile and developing states with a view to enhancing global security. Despite being one of the critical issues on the global agenda today, our understanding of how to successfully state-build remains sketchy, however. ¹ We still struggle with fundamental questions such as how to transfer strong institutions and how to build social capital. To answer some of these unknowns and address the key shortcomings at hand, I will argue that the international community direly needs to rethink its state-building strategy by drawing from recent experience. Key development donors such as the European Union (EU) continue to miss valuable lessons that can be drawn from its very doorstep, where Kosovo and Bosnia & Herzegovina, two of the most significant post-conflict state-building projects of recent times, can teach us much.

A Balancing Act: Top-down or Bottom-up?

The first major problem with current state-building strategy is its failure of approach. State-building can generally be conducted in two ways. The first is a “top-down” approach, where external actors try to stabilise a state by establishing democratic governance institutions, courts and a security framework, aiming for democratic norms and values to trickle down. The second is a “bottom-up” approach, which, by contrast, focuses on establishing stability from a grassroots level, through the construction of social capital and the strengthening of civil society.² It emphasises the importance of cooperative societal relationships and local participation at the base of a functioning state.³

Between the two, the top-down approach has been the option overwhelmingly chosen by the international community. However, inadequate results from this approach show that top-down state-building rests on critically limited assumptions.

By assuming that exporting and imposing institutions is the most effective way to design a state, top-down state-building ignores complex local issues such as social cohesion, cultural narratives and identity. Failing to take these issues into account from the outset means that they later have the potential to undermine the entire state-building process.
This has been a clear issue in Kosovo, a heavily disputed territory between Serbia and Albania. Following the Kosovo War in 1999, the United Nations (UN) implemented a broad scheme of institution-building to stabilise the state, while the EU launched the EULEX mission in 2008 to foster the rule of law. However, Lucia Montanaro identifies numerous local factors causing fragility in Kosovo that have failed to be considered in designing the post-conflict state.¹ Issues of inward-looking social capital, very little history of public participation in governance, and a culture of loyalty to one’s clan or region have largely been ignored by international actors. However, these circumstances have created the elitism and local divisions that have made Kosovo’s imposed governance institutions stagnant and corrupt.² Today, ruling elites exploit public resources for the benefit of their own clan, party or region while paying lip service to good governance, and local communities have little part in political decision-making.³ Fifteen years on from the first state-building intervention in Kosovo, many of the institutions built have been subverted, and Kosovo remains a fragile state.

This experience is not unique to the Kosovo project, and much criticism has emerged about top-down state-building in this regard. Michael Wesley argues that the fundamental failure of this approach is its assumption that the state is an independent variable that can be built, divorced from the context of politics, the economy and society.⁴ However, local behaviours and experiences of these shape institutions just as much as institutions can shape behaviour.

The Kosovo experience shows us that international actors must do away with the ‘one size fits all’ idea of exporting institutions, and must instead adopt a more inclusive, bottom-up approach to state-building that forms institutions based on local traditions of politics, economics, culture and participation.⁵ Without this, achieving stability is unlikely.

**Staying Focused**

As the old adage goes, Rome was not built in a day, and a cohesive and stable democratic state certainly cannot be either. State-building requires a concerted and long-term effort, as the trickling down of democratic norms into local behavior can take decades. However, it is often difficult to sustain the interest of the international community for such extensive periods of time. A second major shortcoming in current state-building strategy is that despite beginning a project with both funds and interest, international actors often fail to maintain the strength of their state-building efforts. Instead, commitment eventually wanes and short-term fixes are prioritised over laying the complex blocks for long-term stability.⁶

We can find a clear example of this in Bosnia & Herzegovina (BiH). In 1995, the devastating Bosnian conflict was brought to an end by the Dayton Accords, crafted by Western powers.⁷ The agreement was the beginning of an external state-building effort. It established a ‘consociational’ constitution for Bosnia in which Bosniaks, Bosnian Croats and Bosnian Serbs each have separate representation.⁸ However, it is widely conceded that the state-building effort in Bosnia has failed to create a stable, liberal state. Instead, the process has been derailed by constitutional troubles, and the divergent goals of the international community and local leaders, amongst other issues.⁹ After continuous setbacks, what began as a project with much backing has over time dwindled, and today the primary

> top-down state-building ignores complex local issues such as social cohesion, cultural narratives and identity.
ongoing contributor is the European Union. Even then, Laurence Cooley writes that the EU has scaled back its hopes for the state, and has largely given up on long-term reform and concentrated state-building efforts. Instead, its focus has been on incorporating BiH into the EU, but even this strategy has been pursued without much conviction, perhaps owing to enlargement fatigue. As BiH struggles with unresolved constitutional issues and a lack of international interest, its predicament illustrates that losing focus in a state-building project leaves a state with new institutions in great number, but also with troubling issues of fragility that go unresolved.

Above all else, Reconciliation

The most fundamental shortcoming of recent state-building strategy, however, is its failure to recognise that states previously divided by ethnic conflict will never be able to achieve a stable, lasting peace without reconciliation. This is because unresolved ethnic division pervades every aspect of the state-building project.

Montanaro writes that ‘reconciliation has not been a priority for the international community’ in Kosovo. As a result, ethnic division has cleaved the new state not only socially, but also politically and institutionally. Tension between Kosovo Serbs and Kosovo Albanians has led to the emergence of a parallel administration, as the northern part of the country, heavily populated by Kosovo Serbs, is entirely directed and funded by Serbia. As a result, the central Kosovo government has struggled to act for the entirety of its territory. Kosovo’s government consistently struggles as political divides along ethnic lines stymie legislative action. Moreover, there has been little trickle-down effect of the rule of law and democratic norms, because there is no unified polity to receive them.

Similarly in BiH, the sad paradox is that the Dayton Accords, which sought to settle ethnic divisions, have instead perpetuated them. Ethnic quotas in institutions have fortified ethnic identities. The International Crisis Group identifies that a three-way fracture between Bosniaks, Croats and Serbs is deeply embedded today in the constitution, judiciary, police, education and the military. Despite, and perhaps due to, state-building efforts, Bosnia remains a perpetually fragmented state in deadlock. Without reconciliation, fostering a civic
culture of democratic participation and commitment to a national polity is near impossible, and where there is no will for peace and stability, often there is no way.

### Back to the Drawing Board

State-building experience in the Balkans offers us several key lessons. Stability is more than just the imposition of liberal democratic institutions. It is not enough to assume that exporting a ‘liberal peace’ framework will, in and of itself, fix causes of fragility such as ethnic division and a lack of widespread participation. Instead, these problems will persist unless the international community adopts a more inclusive, bottom-up approach to state-building, and sufficiently commits to its undertakings. The shortcomings of Kosovo and BiH, but also the successes of Rwanda, show us the importance of reconciliation in post-conflict reconstruction. Despite the uncertainties, by drawing from experience we can inch closer to an understanding of what state-building should be, and how to truly realise a stable and lasting peace.

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Resource Scarcity & Conflict in East Africa:
Ethiopia’s Newest Dam Sparks Concerns

Anne-Louise Knight

International attention on climate change has significantly focused on accelerating the progression to renewable energy sources globally. The three most prominent of these alternatives are: solar, wind and hydro-powered energy production. Hydro-electricity projects through the development of dam infrastructure have become a priority in many African nations since gaining political independence, in an attempt to secure energy independence. However, an ongoing dispute between Ethiopia and Egypt over the Nile River is raising contention over international river regulations and their effectiveness.

Ethiopia has been a prominent hydropower producer, having already constructed 14 hydropower dams and plants.\(^1\) The most recent proposal, announced in 2011, is the Grand Ethiopian Renaissance Dam (GERD). The proposal is not the first Ethiopian hydropower plant to have been built off the Blue Nile River. However, it is the most ambitious project to date, with the plans outlining an installation power of 6000 Megawatts (MW) with an estimated energy output of 15,000 Gigawatts (GWh) per annum.\(^2\) Contesting figures however, suggest that the figures produced by Salini Impregilo (the company responsible for constructing the dam) are exaggerated in an attempt to gain support for the project amidst current upheaval.\(^3\)

The benefits of the dam for Ethiopia seem clear, as the projected energy production would have the capacity to provide domestic energy independence.\(^4\) This would dramatically change the livelihoods of the population of Ethiopia. Currently, approximately 83% of Ethiopians do not have access to electricity.\(^5\) The projected energy production from the GERD is also estimated to produce an energy surplus that Ethiopia will be able to sell internationally.\(^6\) Projections from various economic studies have suggested that the level of Ethiopian economic growth will increase by at least 4% when the GERD begins operations in 2017.\(^7\)

Agreements have already been signed for plans to export Ethiopian power to neighbouring countries, including Kenya, Sudan and Djibouti, with negotiations to supply to Yemen also underway.\(^8\) However, growing opposition from Egypt over water security from the Nile is gaining international attention. Over 85 million Egyptians depend on the Nile for the majority of their water needs.\(^9\) The Egyptian Ministry of Irrigation claims that 20-30% of Egypt’s share of the Nile will be under threat with the operation of the GERD.\(^10\) This is compounded by a projected decrease of 33% in Egypt’s High Aswan Dam energy production.\(^11\) Figures estimate that 70% of the Nile River flow stems from the Blue Nile River in Ethiopia.\(^12\) However, Ethiopian officials have asserted that no disruptions will be made to downstream Egyptians.\(^13\)

Spokesman for the Egyptian Foreign Ministry, Badr Abdelatty, told the BBC that the issue is “a matter of life or death, a national security issue that can never be compromised on”.\(^14\) This demonstrates the fears felt by a majority of Egyptians over water and agriculture security for the future.

Concerns over long-term environmental risks are not only being felt in Egypt. The rural population of Ethiopia (roughly 84%) relies primarily on subsistence agriculture for their livelihoods.\(^15\) This is being placed at risk by the Government’s oversight of long-term environmental factors in implementing hydropower projects.
Studies from the International Rivers Organisation (IRO), an American NGO, state that approximately 10% of the world’s population are negatively affected by dams. This percentage incorporates those who are displaced by reservoirs, lose access to water and food sources, natural resources, diseases and hydrological changes brought about downstream of constructed dams. In addition to the impacts on humans, the IRO has also outlined the major environmental impacts that occur as a result of dam construction. The most prominent of these include the transformation of water composition, altered water flows, prevention of sediment flow, riverbed deepening leading to river bank erosion and lower ground water tables, increased greenhouse gas emissions and the extinction of animal and plant species. However, the current understanding of the GERD’s impact on downstream areas is too limited to conclude that the IRO’s findings would apply to the Nile.

The World Commission on Dams (WCD) issued a final report in 2000 on dam constructions, which analysed the developments of dams and outlined regulations for future dam construction. The regulations are still merely an international guide, however, despite efforts from a number of governments – Germany, South-Africa, Vietnam, Nepal and Sweden in particular - to implement the WCD framework into national policy. However, these policies are still not internationally binding. This reduces the scope for conflict resolution where disputes arise over dam construction, such as the current disagreements between Egypt and Ethiopia concerning the GERD.

The most recent accord over the Nile Basin Reserve was the Nile Basin Cooperative Framework Agreement, signed in 2010 by the upper riparian states. However, this treaty was opposed by Egypt and Sudan. The increased dam production in the Nile by Ethiopia since the signing of this agreement demonstrates the changing political balance of power in the region.

The European Union (EU) has stated that it will not aid in funding the project. The initiative is currently being funded predominantly through Ethiopian bonds and tax revenue. Additionally, the EU has publicly announced its support for Egypt, which is seeking international assistance in relation to this issue. The EU ambassador for Egypt, James Moran, recently stated that the EU intends to help Egypt in light of the recent increase in instability within areas of general poverty. This is also a particularly important issue in the context of Egypt’s presidential poll, which is scheduled to take place in May.

The implementation of the GERD in the Blue Nile highlights the transformation that Ethiopia has undergone in the last 20 years. The scramble for energy independence in East Africa is marking the region’s economic future. Furthermore, initiatives such as the GERD demonstrate a shift in regional political power shift since the race for energy independence emerged. Some view this as an avenue for East African nations to escape the poverty cycle and emerge as international economic powers. However, the progress and success of hydro-electricity projects in the region also demonstrate the inequality of rewards and costs in these endeavours. The GERD project dispute ultimately highlights the unfolding debate of whether the regulation of dam building should be implemented into international law, and suggests a growing need for this as water scarcity and resource conflicts appear set to rise in the near future.
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Towards a Unity Government: Is a Hamas and Fatah Reconciliation Possible?

Megan Fung

Since August 2007, the Palestinian territories have been divided into a Fatah-dominated Palestine Liberation Organisation governing the West Bank and a Hamas-controlled Gaza. This split has presented a significant obstacle to achieving a resolution in the Middle East Peace Process. It arose following a failure of Hamas and Fatah to negotiate a power-sharing deal in government after a Hamas victory in the legislative elections of January 2006. Although tensions had begun to flare between the two factions after the death of Fatah leader, Yasser Arafat, in 2004, it was not until after the election that the conflict intensified and eventually escalated into an outright civil war. Despite this, both Hamas and Fatah have recognised that Palestinian statehood, a common goal despite their ideological differences, would be impossible without the involvement of the other. Much has been made of the latest attempt to negotiate a Fatah-Hamas reconciliation deal, announced on 23 April 2014. With Palestinian President Mahmoud Abbas and Hamas leader Khaled Meshal set to meet for the first time since the failure of a previous delayed reconciliation pact in Cairo in January 2013, this latest attempt is promising. However, it remains to be seen whether external forces will permit a reconciliation to play out or if they will worsen the divide as before.

Compare the Pair

The relationship between Fatah and Hamas is a complicated one. The divisions between these two main Palestinian political factions are deeply rooted in their historical and ideological differences in objectives, governance and relations with Israel. During the period of the Oslo talks, they were fierce competitors, as Hamas considered Fatah’s agreement to recognise the right of Israel to exist to be counter to the true cause of the Palestinian people. Hamas had also been critical of the PLO for renouncing violence and recognising Israel in 1993 without securing firm commitments in return on what a final peace agreement would involve.

Furthermore, Fatah’s legitimacy was considerably eroded by Arafat’s inability to control the various armed factions, such as Hamas and the Islamic Jihad, in his role as head of the Palestinian Authority (PA), as well as the rise in corruption within Fatah and little improvement in the living conditions for ordinary Palestinians. In comparison, Hamas’ social welfare projects had been highly visible in delivering infrastructure such as mosques, hospitals
and schools, which began to strengthen their support base within the territories and their viability as a political alternative. Despite Fatah historically being the dominant political force in Palestine, 1993 onwards marked the beginning of its decline within the Palestinian territories, and the progressive rise of Hamas’ popularity and credibility.

The competition of the 1990s would characterise the rivalry between the two dominant Palestinian liberation movements, although the Second Intifada did see cooperation between the two groups. The legitimisation at the elections of Hamas’ involvement in Palestinian politics, and the resulting necessity of power sharing, threatened Fatah’s traditional political monopoly and catalysed the violence between the two that escalated into the 2007 civil war.

Gaza’s Isolation

Some believe that the primary beneficiary of Hamas’ distress is Fatah, who hoped that Gaza’s isolation would see the toppling of its rival. However, although politically isolated and in severe economic distress, Hamas’ hold over Gaza has not weakened enough to allow Fatah to regain control over the territory. In fact, Hamas has been credited with establishing an entrenched governing apparatus, with a fully functional judicial structure (albeit imperfect), that can draft a modest amount of narrow legislation under these conditions. In addition, Hamas has shown an ability to negotiate ceasefires with Israel through third parties, such as Egypt, and often acts with force against those who violate them, particularly those without the “cover” of membership in an established organisation.

Nevertheless, periodic escalations of violence between Israel and Gaza continue to occur, with the last major escalation (known in Israel as ‘Operation Pillar of Defence’) unfolding in November 2012. The possibility of another escalation of violence between Israel and Gaza is a real possibility, given Gaza’s difficulties and economic constriction. This is something a weakened Hamas cannot afford. A consideration of these factors may hint at the causes behind Hamas’ willingness to reconcile.

Political Pragmatism

Despite their differences, both sides have revealed themselves to be pragmatic actors motivated by a sense of political realism. Hamas had already shown signs of moderation in the lead up to the legislative elections, contrary to its public discourse; the faction made concessions to preserve the movement’s political assets without blurring its ideological distinctiveness. Since then, Hamas’ governing responsibilities in Gaza have also made it directly accountable to its voters, requiring it to maintain a functioning civil society under complete isolation and a blockade imposed since mid-2007. Fatah leader Abbas has previously stated that any negotiations with Hamas can only be conducted after they acknowledge their “coup”. However, he has similarly come to the negotiation table, in recognition of the importance of a united front for securing Palestinian statehood, and frustrated with a lack of progress in US-brokered peace efforts. Hamas’ Meshal has also noted that Hamas would be willing to negotiate on a two-state solution based on 1967 borders, so there is mutual ground between the two movements and room for dialogue. This recent reconciliation deal is ambitious, with the target date for forming unity government set at one month, and elections to follow within six months. However, it is certainly not impossible.
The External Factor

It remains to be seen to what extent international actors will involve themselves in the latest reconciliation attempt. It was Hamas’ inability to accept the Quartet’s principles in 2007 that drove it away from integrating democratically into the Palestinian political system, and that may very well occur again. Israel and the US have made it clear that they will not deal with a Palestinian government backed by Hamas. However, the European Union has issued a more moderate statement that the EU has “consistently supported intra-Palestinian reconciliation, but on clear and certain terms”.

Nevertheless, Fatah’s announcement of the reconciliation deal with Hamas five days before ongoing negotiations with Israel were set to expire is no coincidence. With both sides of Palestinian politics expressing their disenchantment with the lack of progress in peace negotiations, this may just be the impetus they need to finally secure a successful unity deal between them.

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Between a Rock and a Hard Place: Should the United States intervene in the Democratic Republic of the Congo?

Rachel Stone

After two centuries of colonisation and Africa’s ‘World War’ of the late 1990s, the Democratic Republic of the Congo (DRC) has struggled to stabilise as a nation. Despite a peace deal and the formation of a transitional government in 2003, the country’s vast mineral wealth has attracted a host of interest groups, some predatory, and the people of the nation face ongoing terror from local militias and the army. On the governmental side, endemic corruption, poor infrastructure, and an uneasy leadership have not made for peaceful progress. A rift between the currently-serving President Joseph Kabila and his allies sparked a rebellion in the early 2000s, with both sides supported by different neighbouring countries. This instability has failed to dissipate, and the question of whether the DRC needs a stronger nation to intervene and shoulder its seemingly inescapable burden has emerged. At present, the DRC is home to the United Nations’ largest peacekeeping mission, but many have considered the United States (US) as the most fitting contender to stage a military intervention in the DRC to establish order and re-build the state. However, this proposition does not consider the complexity of intervention for the US, whose ideological and recent history shows a withdrawn attitude towards African affairs. In lieu of the US, China has been put forward as a suitable alternative to lead a stabilising intervention. This idea must also be treated with caution, however, as China does not seek to take an all-encompassing grasp of the DRC’s future, and will try to keep its relationship with the DRC predominantly on business terms.

Of a half mind

There are both historical and current substantiations to suggest that the US has little desire to intervene in the Congo.

Historically, the policy towards Africa undertaken by previous US administrations has been half-hearted and without conviction. American leaders have used positive rhetoric and statements of hope for a democratic DRC led by good governance, but consistently trend back to the Jimmy Carter administration, which pressed the point of self-determination. “Africa’s future is up to Africans”, Barack Obama stated in a speech to the Ghanaian Parliament in 2009. Looking to current events, it is unlikely that President Obama would be able to sway the American public and US Congress towards such a venture. Even with the weight of a second election no longer acting as a constraint on Obama’s decisions and the fear of not being re-elected now allayed, he will be seeking to...
depart with a positive legacy for, as the Democrats hope, the next Democratic President. Over the course of Obama’s two terms, he has been seeking to wrap up the hugely unpopular US interventions in the Middle East. Domestic sentiment has been decisive; a recent national survey conducted shows that 66% of Americans today oppose involvement in the conflict in Afghanistan, believing that ‘it has not been worth fighting’, as the means outweighed the gains. Moreover, with the recent movements of Russia in the Crimea heating up tensions in Eastern Europe, and the competitive trend in Sino-US relations, Obama’s time and energy will be stretched between the two regions for a large part of the rest of his term. It is unlikely that he would seek to sell another intervention endeavor, and it would be a departure from how the US has traditionally acted towards African affairs.

An economy on the rise

Following the 2008 Global Financial Crisis, the US has somewhat recovered from its economic fall, and economists agree that 2014 will be a better, if not a good year for the US. However, despite the American economy being on the mend, foreign interventions are a highly costly exercise and require an unwavering commitment that the US is unlikely to give.

To date, Afghanistan and Iraq collectively have cost approximately US$6 trillion. Reconstruction in Afghanistan alone has cost US$87 billion. To add further insult to injury, after all the money and time spent, opinions on the outcome are mixed and mostly critical. However, this is nothing new. As Sara Kasper and Minxin Pei argue, out of the entirety of US military interventions since 1900, only two have been unambiguously successful. Kasper and Pei frame ‘success’ as an intervention culminating in a ‘nation-building’ stage with lasting democratic results. Against the tall orders of time and expense, however, the US will be hard-pressed to see the DRC through to this stage.

Moreover, recent reports indicate that China will soon be poised to surpass the US as the world’s leading economic power. While the loss by the US of its top economic status does not mean the loss of its considerable cultural influence and soft power, strategically, US leaders would do well not to spread the US profile too thin and become weak. Thus if there were ever a time for the US to become involved in the DRC, it would not be now.

East Asian trees grow taller

It has been suggested that a better candidate to lead a reconstructive Congolese intervention is China. Indeed, China has economic power, military might and a higher level of engagement with the DRC. In comparison to the US, China’s aid model does not consist of donations, but works as an investment strategy providing the long-term benefits of jobs and sustainable development. In 2008, China overtook the US as Africa’s largest trading partner, making itself a more established influence across the continent. It is possible, as Sean Lavelle argues, that the US could play a dual role with China in the DRC, but Lavelle has not factored in the current circumstances of the US, nor its previous record with Africa. The cooling of relations between the US and China adds another impediment to this proposition.

However, supplementing a US intervention with a Chinese intervention is by no means a simple or valid solution. Certainly, China’s ventures in the DRC have involved considerable investments in the country’s mining sector, and Beijing has agreed to hire local Congolese workers and provide aid to address social needs, in an attempt to muster local support. However, China has not gone further to tackle the root causes of the security problems in the Congo, such as crippling corruption amongst the political elite and the lack of tangible economic benefits for the Congolese people. As realists would posit, states will always act in their own

“... states will always act in their own self-interest and ultimately, investments are designed to benefit the source.”
self-interest and ultimately, investments are designed to benefit the source. China’s relationship with the DRC is primarily of a business nature, and its economic pragmatism will not fix a troubled nation.

Self-dependence

So perhaps it is more fitting for the DRC to walk this path alone. Between the US’ wavering assistance and China’s questionable intentions, there are few other superpowers who could or would stage an intervention to reconstruct the DRC. The US will likely be occupied by its domestic agenda, and focusing on tempering the hostility in Russia and in Northern Asia. Moreover, drawing from its history, the US has traditionally stayed away from interfering in Africa, and its rare incursions, such as in Somalia, have been unsuccessful, leaving little precedent or incentive today. For China, involvement in the DRC appears to be a work of market expansion and a resource venture to prop up its steady economy. Despite the advantages of this trade relationship for China, the DRC’s progress in its struggle for stability is unlikely to drastically improve as a result of this business relationship. Instead, the nation may simply continue to stagnate unless another, more sustainable and substantial, alternative for intervention or reconstruction emerges.

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The New Energy Era: A Cause for Optimism

Nicholas Gurieff

Considering the commentary on climate change in the media and academic literature, it is often easy to be pessimistic about our prospects as a species on Earth. The warnings about climate change grow more urgent by the day, and common reports paint a bleak picture of governments, and an increasingly apathetic citizenry, failing to act, and of people being more concerned with short-term economics than long-view science. Simply, we see the image of an overwhelming task that is all but insurmountable. I will argue that a large part of the change we need is not only possible but inevitable, and that the pessimistic outlook we are often fed ignores the changes that society has achieved in the past as well as the contemporary trends that are currently unfolding. Importantly, there seems to be much foundation for the assumption that most people want to go on living as they do now with a comprehensive lack of imagination and vision. I would like to use this article to reveal the world as I see it – an outlook inspired by the ideas of Amory Lovins and Jeremy Rifkin, backed by the transformations around the world as reported on by media new and old.

The Vision

Lovins reveals his vision for 2050 in his book Reinventing Fire: Bold Business Solutions for the New Energy Era. A world with an invisible yet omnipresent support structure of smart technology, with super-insulated houses and efficient appliances, electric cars and community energy, natural lighting and fresh air, onsite manufacturing and decreased military conflict. It ties into Rifkin’s vision of the ‘Third Industrial Revolution’, explained in his 2011 book. The narrative Rifkin weaves centres on the combination of new communication technology with novel energy systems, referring to a shift that is ‘conceptual rather than technical in nature’. This appears accurate, as we have created much of the technology we need already. He concedes the ‘considerable task’ we face but reminds us that the historical transformations from wood to coal power, and from coal and steam to oil and electricity, were achieved in half a century.

Communities, businesses and governments are envisaging similar developments. Among the top goals outlined in a 30 year vision for the state of Queensland, created by the community through a State Government initiative, are that “we invest in and adopt sustainable and renewable solutions”. When asked “what does...
success look like?” in achieving that latter goal, Queenslanders have said, “renewable energy will be the norm.” Coal ‘is nowhere to be found in the draft Queensland Plan’, which is astonishing when you consider that coal is the state’s largest current export earner. Then there is the US business ‘Climate Declaration’ signed by 40 major companies and more than 100 others, including investors, who see climate change not only as a challenge but also an opportunity. On the nation-state level there is the world’s biggest oil producer, Saudi Arabia, which is planning a ‘100% switch from fossil fuels to clean energy’. These are but a few examples.

**The Transformation**

These aspirations are not confined to the realms of fantasy; Lovins’ vision is already playing out. At the community and local government level we have created buildings designed as
ecosystems, built metro train stations that generate half of their own power from solar, and rolled out iconic electric taxis. Communities are taking control of their own energy, as are individuals and businesses, with renewable energy and big batteries. There are more than 600 energy cooperatives in Germany, while in Denmark, a country that generates a third of its power from wind-energy, about 86% of that production is locally owned. More Kenyans get first electricity now from solar than the grid. At the national level, Uruguay is replacing their buses with electric versions, and China ‘outstripped even the most optimistic forecasts of 12 months ago’ with solar installations in 2013. Saudi Arabia, backing up their previous announcement, this year broadcast ‘plans to invest $109 billion to produce 41 gigawatts (GW) of solar energy by 2032’.

The private sector is pushing ahead too. Major utilities in the US are installing solar and wind because they are cheaper than fossil fuel power stations, while those in Germany that preferred installing new coal capacity over renewable investment have admitted to making a costly mistake. ‘Microsoft will buy the entire output of a Texas wind farm’ and ‘Google now has five such agreements in place’ purchasing hundreds of megawatts of renewable energy. Toyota, the world’s largest car manufacturer, is launching a hydrogen fuel-cell vehicle. Apple has extended ‘free recycling to all used products’, its four data centres now use only renewable energy, and ‘roughly 94 percent of the power used by Apple offices across the world is now from renewable sources’.

Our technology is also getting smarter. One of the largest wind turbine manufacturers is creating intelligent turbines that self-optimise, while German energy utility company RWE, facing declining revenues from fossil fuel plants, is ‘teaming up with one of Google’s recent acquisitions, Nest Labs, which makes internet-connected thermostats and smoke-d Detectors’. Car companies are focusing on software and creating new electric vehicles out of carbon fibre. Money is being made in the process too – ‘the energy-conservation business is booming’ with sales of sensors and network technology related to the application of efficient LED lighting set to grow from $1.1 billion in 2013 to $2.7 billion by 2020. In a sentence – ‘Amory Lovins was right’.
Conclusion: the conceptual shift and the beginning of a new era

One example of the negative media commentary I made reference to is a recent New York Times editorial focusing on the upcoming 21st Conference of the Parties. The editorial refers to ‘exercises in futility’, ‘daunting’ tasks, ‘ominous’ reports and a lack of ‘public anxiety’. I, however, see the world already beginning the revolution we need. I see an Apple CEO angrily defending environmental initiatives, the world’s most powerful military powering its bases using renewable energy, and investors viewing coal as the new tobacco. I see major energy utilities changing business models to avoid a ‘death spiral’ and fossil fuel company PR campaigns ironically firing up protesters instead of supporters. I see McKinsey discovering the ‘disruptive’ potential of solar, and a subsidiary of legendary US investor Warren Buffett buying $1 billion of wind turbines because it is the cheapest form of generation, in doing so creating the state of Iowa’s ‘largest economic development effort in history’. I see top superannuation funds like UniSuper adding fossil fuels to a list of unethical investments, and an anti-apartheid style boycott of the fossil fuel industry backed by Nobel Peace Prize winner Desmond Tutu. In the words of Peter Bijur, once chairman and CEO of Texaco, from the World Energy Council keynote in 1998: ‘The arguments for marginal, incremental change are not convincing – not in this day and age. The future, after all, is not linear. History is full of sparks that set the status quo ablaze.’ I do not advocate complacency, as we still have a great deal of work ahead of us, but I do argue for a healthy dose of optimism. While we may not be able to avoid significant, detrimental environmental changes around the world, we can likely prevent catastrophe and come away from a clean energy transformation better off in many ways. We have already witnessed societal transformation founded on energy revolutions and we can do it again. We have, in fact, already begun.

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Fusion Power: Endless Energy
Adam Ingle

Star Power

Imagine an energy source more abundant than coal, safer than nuclear reactors, greener than solar and almost entirely self-sustaining. It sounds too good to be true – and it is, for the time being.

Human attempts to harness nuclear fusion – the process that powers the Sun and other stars – have stuttered along since the idea was first conceived in the early 20th century. Fusion occurs when ions of hydrogen or its isotope momentarily combine (fuse) then spilt to create helium nuclei, releasing vast amounts of energy in the process. It is actually an application of Einstein’s famous $E = mc^2$.

Although it sounds deceptively simple, fusion is impossibly difficult to replicate. Requiring absurd amounts of heat (150,000,000°C, ten times hotter than the Sun’s core) and precise levels of energy confinement, man-made fusion lasts for a fraction of a second. It was only in September 2013 that scientists were able to create a reaction that released more energy than it absorbed, the holy grail of fusion research. The fantastically named physicist Omar Hurricane and his team at the National Ignition Facility (NIF) in California generated about 15 kilojoules of energy from an input of 10 kilojoules. To put this into context, 10 kilojoules is roughly the amount of solar energy received by a square metre of Earth over 10 seconds. Little as that seems, it is a small step in the right direction.

A True Panacea

Consider that global population is projected to increase by 2.4 billion by 2050, accompanied by a 56% increase in world energy consumption due to the rapid industrialisation of developing countries. Current estimates suggest that global oil reserves will expire in 2052, with gas reserves following in 2061 and coal reserves depleting by 2088. Consider also that the uranium required for traditional nuclear reactors is finite, hazardous and expensive to extract. Uranium’s more benign cousin thorium is subject similar limitations. Alternative power sources such as hydro, wind and solar struggle to produce the same quantity of energy as fossil fuels and are subject to the caprices of weather.

Fusion energy does not suffer from any of these shortcomings. The principal fuels that power the reaction, deuterium and tritium, are abundant and accessible. Huge quantities of deuterium are present in water and can be easily extracted at little cost. Due to a fast rate of decay, tritium isn’t so plentiful. However, it can be gathered from subjecting lithium – a common metal used in mobile phones and laptop batteries, and also present in water – to the fusion process. Amazingly, tritium can also be harvested from the very reaction it fuels.

Only minute quantities of each are required to power the fusion process. A coal-fired power station burning ten thousand tonnes of coal creates the same amount of energy as a fusion reactor using one kilogram of deuterium and tritium. In other words, the fuels extracted from one laptop battery and 45 litres of water would produce similar levels of energy as 70 tonnes of coal, enough to satisfy an average person’s consumption needs for 30 years. It would take millions of years to exhaust the terrestrial reserves of deuterium and tritium.

As the processes required to power fusion occur on an atomic level, it is a form of nuclear energy. Yet because the energy is generated by fusing atoms, rather than splitting them as with traditional fission reactors, it is intrinsically safe. Given that fusion is so difficult to sustain, the instability that otherwise risks unmitigated disaster in fission reactors would merely cease the fusion process with little or no consequence. Any radioactive material produced would be short lived, lasting 50-100 years rather than thousands, and the radioactivity could be confined to the power plant itself as storage and waste disposal is not needed. A world powered by fusion...
would see the threat of disasters such as Fukushima and Chernobyl disappear completely.

That is not to say that fusion itself is problem free. Aside from the difficulty of sustaining a reaction, few materials can survive the extreme conditions created by one for a prolonged period. Intense laser blasts and massive amounts of heat degrade reactor walls faster than a commercial operation could tolerate. New materials such as graphite and carbon fibre may provide an answer but until this challenge and others are overcome, fusion will remain a scientific pursuit.

The Way Forward

Governments have appreciated the potential of fusion power for decades, although only recently have we seen fusion research transition from a laboratory to an industrial scale. The International Thermonuclear Experimental Reactor (ITER) is a €15 billion collective effort by China, the European Union, India, Japan, Korea, Russia and the United States to build a demonstration fusion power plant in France. ITER will use specialised magnets to create and control the ‘burning plasma’ that drives the reaction. Alternatively, Mr Hurricane and his team at the NIF attempt use ‘ignition’ to start the reaction, focusing 192 lasers at a golden pellet. Two more projects, the DEMOnstration Power Plant (DEMO) and the International Fusion Materials Irradiation Facility (IFMIF) are under development pending the success of ITER, which is to become operational in 2020. Although these projects may sound impressive and enticing, fusion research received little more than €750 million in funding from the EU from 2002-2006 and only $248 million for 2013 in the United States, numbers which pale in comparison to the hundreds of billions in defence funding for example. If necessity is the father of invention, one hopes he would give his children more pocket change. Nevertheless, the volume of major projects in the pipeline reflects the urgency of our situation. Resource scarcity is a catalyst for modern conflict and we can expect competition for fuels to increase as traditional sources dwindle. The current Ukraine crisis can be, in part, seen as a competition to secure Russian gas resources while the role that oil has played in Middle Eastern conflicts is widely acknowledged. Crucially, as anthropogenic climate change continues to develop, crop yields and water supplies will diminish; competition for these resources will also increase. Abundant and emissions free, fusion provides a solution to these impending problems. Scientists often joke that fusion power will perpetually remain ‘only 30 years away’. Given the scale of our resource challenges in the 21st century one can only hope that this time it actually is.

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On 5 June 1981, the United States Centres for Disease Control and Prevention published a report of very unusual clusters of homosexual men affected by a rare form of pneumonia previously seen only in severely immunocompromised patients. With the benefit of hindsight, we can now argue that few other things have struck as much fear into our collective consciousness as the cause of these aforementioned, otherwise rare, infections - the Human Immunodeficiency Virus (HIV). Now known as the virus which causes AIDS (Acquired Immunodeficiency Syndrome), this disease has managed to transcend race, sex, sexuality, age and indeed almost every other divide one may think of, currently infecting over 30 million individuals, resulting in two million infections each year and causing 1.7 million deaths worldwide.

In 2000 a major step was taken by the international community in declaring the eradication of HIV/AIDS as a pillar of the United Nations’ Millennium Development Goals (MDG). A series of high-level meetings breathed life into the specific points of this lofty and, according to some, ambitious goal. These included the reduction of sexual transmission of HIV by 50% or more by 2015; eliminating HIV infection amongst children; reaching in excess of 15 million patients living with HIV through life-prolonging anti-retroviral therapy; halving tuberculosis deaths amongst sufferers and eliminating the stigma, discrimination and punitive laws associated with the disease. But thirty years since the discovery of HIV/AIDS, and fourteen years on from the elaboration of this MDG, just how well are we faring?

The latest epidemiological data comparing 2001 to 2012 are promising. Over this period, new HIV infections have dropped by 1 million per year, from 3.5 to 2.5 million, with a significant decrease in the number of HIV-related deaths and parallel increase in the number of individuals living with the illness. While any small victory must be seen in the broader context of the still-overwhelming numbers afflicted by this disease, these developments provide us with hope that prevention, awareness and treatment campaigns are being implemented with some success. From 2001-2012, 26 countries have halved the incidence of HIV/AIDS by over half, with a similar 34% decline in rates within sub-Saharan Africa. But what are some of the forces which continue to stifle our ongoing efforts?

A major barrier to more effective reduction in the global incidence of HIV/AIDS is the difficulty encountered in changing social attitudes towards the disease. These attitudes are paramount: they influence sexual practices at a grass-roots level, they influence who gets tested for the virus and also who will seek treatment. While a global meta-analysis demonstrates that behaviour interventions may reduce risky sexual practices and thereby control the spread of
HIV, it is similarly true that many countries, particularly poorer ones, often do not have the necessary institutions or social capital to successfully implement these campaigns.\(^5\)

Fear of social stigma, criminalisation and social inequities continue to form barriers to changing uninformed or misled attitudes towards testing and its vital role in HIV prevention. A landmark qualitative survey of attitudes towards testing taken of 500 individuals from Cape Town, South Africa, a country in which there are 1,500 new HIV infections every day, demonstrated that of all individuals surveyed, 53% had been untested. These patients had more AIDS-related personal prejudices, were more likely to believe that HIV/AIDS was a “dirty” disease for which one should feel ashamed, and were more likely to feel that it was a consequence of immoral actions.\(^5\) An earlier study by Stall et al. who studied the attitudes to testing demonstrated that approximately two out of every three men who have sex with men, unaware of their HIV status, suggested that social stigmatisation contributed to their choice not to be tested, including fears of isolation and rejection.\(^7\) It is very clear that changes to social attitudes towards the disease are paramount in overall efforts to control its spread.

HIV/AIDS places a disproportionate burden on the poor and the disenfranchised while accentuating and indeed aggravating social and gender inequalities. So long as the conditions exist in which HIV/AIDS may be spread and the epidemic continues, such inequalities will likewise remain. Nowhere is this more apparent than in the case of women, who account for over half of HIV-1 infections worldwide. From 1999 to 2003, the annual number of AIDS cases increased by 13% in females compared to 1% in men.\(^8\) In South Africa, one in four women are infected by their early 20s.\(^9\)

Why do women in particular carry an unequal burden from HIV/AIDS, where stigma may have a negative impact on an individual’s social interaction, employment, self-esteem and motivation to adopt health-promoting behaviours, including the decision to get tested and seek treatment?\(^{10}\) Power inequalities, particularly in heterosexual relationships, can often create a culture of silence regarding female sexuality, stifling the ability of women to become health literate and thereby inhibiting their protection from HIV infection.\(^{11}\) The pervasiveness of myths regarding female sexuality, particular but by no means exclusive to developing countries, include widespread fears of condoms and the idea that intercourse with female virgins may cure a man’s HIV infection. This speaks to the ignorance – much of it inadvertent – that many experience due to inadequate access to education and low socio-economic status.\(^{12}\)

Gender-based violence or even the threat of it may also have a crippling effect on a woman’s ability to negotiate the terms of their relationships and their sexual experiences. Such is the ubiquity of such violence that this form of inequality and subsequent predisposition to HIV infection is not simply limited to areas of the world in which the rule of law has been undermined, or where the use of rape and sexual violence may be used to achieve political ends. Rather, it is a very common problem, in developed countries as much as developing, where the fear of domestic violence (and perhaps the fear of losing socio-economic security) may negatively impact one’s ability to negotiate the terms of their sexual encounters, including condom use and disclosure of

“A major barrier to more effective reduction in the global incidence of HIV/AIDS is the difficulty encountered in changing social attitudes towards the disease.”
HIV status.\textsuperscript{13} This association has been researched empirically in a large range of studies examining exposure to intimate partner violence in HIV-positive and HIV-negative women, particularly in Sub-Saharan Africa. These studies have consistently demonstrated a positive association between domestic violence and risk of exposure to HIV/AIDS.\textsuperscript{14}

It has been over thirty years since the HIV/AIDS epidemic was first identified, and while marked progress has been made in the areas of primary, secondary and tertiary prevention, it very much remains the great global health challenge of our age. In order to more effectively tackle the scourge of this insidious but devastating infection, it is necessary to address its social dimensions. We must change the punitive attitudes to HIV infection, where resulting stigma hinders efforts to encourage individuals to be tested and seek treatment. We must change the culture of silence surrounding sexuality and instead promote health-affirming behaviours so that individuals, particularly those who are poor or of low socioeconomic status, are able to protect themselves from infection. We must remedy the power imbalances in human relationships that perpetuate intimate partner violence and are associated with HIV status. It may seem like a large task, but it is an essential one; it is clear that we must shake the injustices that continue to mar human progress, lest we continue to live with its destruction.

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Stateless in Kenya: 
The Plight of Kenya’s Internally Displaced Persons
Kamal Singh

Kenya has long been viewed as East Africa’s most stable democracy, with key economic, military and strategic influence in an otherwise tumultuous and unpredictable region. By 2007, the nation had recovered from the oppressive regime of President Daniel arap Moi and was sustaining economic growth rates of 6-7% with an optimistic outlook. Hence it was with a degree of shock that the world witnessed Kenya descend into horrific ethnic violence verging on civil war following the declaration of general election results in late 2007. Conservative estimates have placed the number of deaths at over 1300, with the displacement of over 600 000 people to add to 400 000 already displaced in previous election violence. This article will aim to present the causes of such violence, the subsequent plight and current situation of displaced Kenyans within the context of long standing turmoil on the African continent.

IDP vs. Refugee: An Important Distinction

Internally Displaced Persons (IDPs) are defined as persons who flee their place of residence due to armed conflict, situations of generalised violence, violation of human rights or natural or human-made disasters, without crossing a recognised international border. Those who leave their homes for similar reasons but cross an international border in search of asylum are considered refugees. This seemingly minor difference has significant implications for health and wellbeing as IDPs, who unlike refugees, are not protected by any binding international protection agreements. There are no international protection agencies for IDPs analogous to the UNHCR and insufficient monitoring of their situation means we have little data on their unique needs. Such is the nature of their plight that Kofi Annan once referred to the 26.4 million IDPs spread across the world, as the ‘most vulnerable of the human family’.

Displacement in Africa

Globally, trends in numbers of refugees and IDPs show an inverse relationship. While numbers were almost equal in 1989, there are now twice as many IDPs as refugees. Nowhere has this shift been more evident than in post-colonial Africa. Between the 1960s and 1980s, Africa had a rightful reputation for the generous treatment of refugees. Displaced populations generated as a result of independence struggles, in most cases, were freely granted asylum with full rights in neighbouring nations, in accordance with the 1969 Organisation of African Unity Refugee Convention. The ideologies of pan-Africanism and anti-colonialism combined with welcome financial support from developed nations (‘burden sharing’) helped drive this ‘golden age of asylum’.

This open door policy has since been replaced with ‘pseudo-asylum’, with fewer and fewer African states willing to provide asylum and settlement opportunities to the displaced. This has been, in part, due to economic pressures, politicisation of asylum seekers and international reluctance to provide long-term support to refugees. As a result, those displaced are now less likely to seek asylum across borders, and more likely to rely on governments whose failure, tragically, may have been the very cause of their displacement.

Kenya’s troubles

Displacement in post-colonial Kenya is a result of the interaction between historical land grievances and the quagmire of ethno-political alliances which dominate multiparty politics in the nation. Land occupies a key position in the Kenyan psyche, presenting a vital link to wealth, welfare, identity and status. In a country where
agriculture is a key economic pillar, the 24% of land that is arable is easily manipulated as a political tool.14

The root of current land grievances, particularly in the Rift Valley, lies in colonial era policies. The British policy of establishing land reserves based on ethnicity helped to embed ethnic identity in geographical space for historically nomadic groups.15 The Rift Valley became the land of the Kalenjin while the Central province was predominantly Kikuyu.

Subsequent policies such as the Swynnerton Plan, designed to provide Kenyans with land for commercial agriculture, served merely to develop a ‘landed’ middle class who were well placed to increase land ownership following independence in 1963.16 The Kikuyu under the first president Jomo Kenyatta (also Kikuyu) were seen to have acquired a disproportionate level of land, expanding beyond the boundaries solidified by colonial policies. Over the subsequent 40 years, this perceived Kikuyu domination has come to dominate land grievances, voiced particularly by the Kalenjin of the Rift Valley.17

The government’s response has been dominated by silence, which has in part helped grievances to resurface around election time through the use of hate speech and intimidation by politicians encouraging further balkanisation of Kenya’s electorates.18 This usually culminates in widespread violence against ethnic minorities or those seen to have transgressed ethnic boundaries. In the Rift Valley in particular, politicians have been known to call for the removal of the Kikuyu madoadoa (stains) to allow the Kalenjin majority to regain access to their land. Such incitement leading to violence has been witnessed in a shockingly routine manner in every multiparty election between 1992 and 2007.19

Other writers suggest that while land is central to displacement, Kenya’s image of stability is in fact brittle and prone to frequent outbreaks of civil violence in the absence of meaningful political reform.20 An often unquoted aspect of Kenya in 2007 was its performance on World Bank Governance Indicators. Kenya was placed below the Sub-Saharan mean in three of the following four areas: government effectiveness (28/28 percent), political stability (15/35.6 percent), control of corruption (16/30 percent) and the rule of the law (5.7/28.8 percent).21 It could be argued that had Kenya teetered on a dangerous precipice, and the contested election result was merely the ignition spark.

**Kenya’s displaced**

Regardless of the cause of the violence, the human cost of Kenya’s instability has been significant. A majority of the 600 000 displaced by the violence continue to reside in IDP camps throughout the countryside.22 Access to basic needs including food, water, sanitation and healthcare continues to be irregular throughout such camps.23 Research conducted by the UNSW 2013 Kenya Team headed by Professor Robyn Richmond from the School of Public Health and Community Medicine revealed alarming health challenges, particularly regarding nutrition, food security, cardiovascular disease and reproductive and maternal health. As their displacement becomes protracted, and hopes for meaningful solutions disappear, it is expected that these public health challenges will have a significant impact on health and wellbeing.

Government initiatives to provide assistance to Kenya’s displaced have largely been lacking. Resettlement programs such as Operation Rudi Nyumbani (Return Home) have been poorly co-ordinated and ignored the fact that most of those displaced do not feel safe going back home.24 In cases where financial compensation has been paid to IDPs, it has been insufficient (10 000 Kenyan Shillings, equivalent to AUD$127) to re-establish lost livelihoods.25
The future?

Kenya, as a signatory to numerous regional IDP protection agreements, is bound to safeguard the economic, cultural, social and civil rights of Internally Displaced Persons. The government of Kenya has taken numerous steps on paper to ensure the wave of violence witnessed in 2007/08 is not repeated. The continuing implementation of the National Accord and Reconciliation Act (2008) has been a positive step to reconcile communities and mitigate against future conflicts. In 2012, the Kenyan parliament tabled a National IDP Policy and Bill. Once implemented, it will become one of only 22 other nations (including 6 in Africa) to have legislation for the protection of IDPs. Efforts need to be made to ensure that such legislative and administrative progress is reflected in meaningful betterment for the futures of the displaced.

Perhaps most pleasingly of all, the 2013 Kenyan General Election was conducted without significant reports of violence and displacement. At its core, displacement and the plight of those displaced in Kenya remains a political problem, and political will is necessary to address it. It is only in this way that Kenya can ensure that the horrific wave of displacement witnessed in 2007/08 is its last.

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Deciphering Social Media in Business Strategy
Abhishek Bhovar

The scale and influence of social media today is enormous. As knowledge continues to grow exponentially, the amount of information processed through these forums similarly grows. Occasionally, an unsuspecting business or organisation publishes material that is considered distasteful by consumers of social media. This was recently illustrated by the New York Police Department and their well-publicised #NYPD Twitter campaign. Having launched the hashtag to promote friendly sentiment towards police, #NYPD quickly became the source of a backlash surrounding the mishandling of locals during arrest and custody. Drawing from this example and several others, this article will explore the factors that produce successful social media campaigns, and the strategies firms commonly use to harness greater economic efficiency and higher revenues through social media channels.

A Tale of Mixed Success

One of the most drastic modern changes in internet usage has been the transformation of people from passive information users into active users who increasingly create the content of the internet on an individual basis. As over 80% of global internet users have access to social media forums such as Facebook, Twitter and Instagram, social media has played a pivotal role in instigating this change. Economic growth has largely accompanied the increasing sociocultural significance of social media, as exemplified by Facebook’s $2.34 billion advertising revenue for the fourth quarter of 2013 alone.

However, the business sector’s increased engagement with this medium has come with mixed success. Californian clothing store Wet Seal credits its Twitter followers and Facebook friends for having a 2.5 times greater sales conversion rate than its average online customers. On the other hand, Qantas Airline’s ‘#qantasluxury’ campaign presented one of the worst social media-based PR disasters in recent times. Qantas launched a Twitter campaign in November 2011, encouraging users to tweet luxury inflight ideas to win first-class amenities. However, customers used the hashtag to post negative tweets instead, reaching over one million people in an hour. These differing experiences of businesses and other institutions in their interaction with social media raise the following questions:

- How is social media different from other forms of communication?
- How can a business tap into the potential of social media?

Setting Social Media Apart

In his article titled ‘Youth Engagement in Singapore: The Interplay of Social and Traditional Media’, Marko Skoric presents a national survey of approximately 2 million Singaporean Facebook users, assessing the basis of their empirical claims when they consider the integrity of information on Facebook. He writes that while traditional information differentiation has predominantly been based on factors such as the news source, frequency, publication date and ‘expert’ commentary, other factors have dominated contemporary considerations of ‘truth-value’ in the social-media context. The most prevalent of these has been the frequency and popularity of particular data within people’s social networks. This was evident in the ‘KONY2012’ campaign, which prompted over four million tweets in three days after its release and 3.6 million pledges to the Invisible Children initiative in the same duration of time. With a single office in San Diego and very little previous coverage of any of its reports, Invisible Children was until then an unknown
organisation to almost all non-American individuals who engaged with the campaign. Its success in these circumstances highlights the role of popularity and general consensus as a form of empirical evidence within the social media sphere. This is based on the underlying assumption that if a large number of similar people support a particular campaign, they must have considered its validity and accuracy when doing so.

The second most distinguishing trait of social media, relative to traditional media, is the subversion of the 'snowball effect'. The snowball effect is a commonly used analogy based on the manner in which a small snowball can, as it rolls down a hill, become significantly larger and more powerful. Until recently, traditional media has been controlled by large organisations which are able to strongly regulate and shape which news items receive the greatest exposure and popularity. However, social media facilitates, with surprising ease, the sharing of alternate information by otherwise voiceless users in a fashion that is of their own interest but can similarly snowball.

Social media has empowered passive users in this sense, as it allows them to propagate individual viewpoints in a widely accessible and far-reaching manner, an ability that was once reserved for traditional media sources.

Lessons in Business Strategy: Market Segmentation and Consumer Engagement

So how does one tap into the potential of social media? Responding to this question has prompted investigation by various organisations on the importance of social media from a business standpoint. Management consultancy firm Bain & Company's recent survey of around 3000 consumers revealed that customers who engage with companies over social media spent 20-40% more on their goods and services. Furthermore, these firms were, on average, rated 33 points higher on the Net Promoter Score, a standardised test that involves asking customers about their likelihood of recommending a company to friends and family. These results justify the average $750,000 annual spending by 'billion-dollar companies' on social media. In their individual studies of the economic potential of social media, global management consultancy firms Bain & Company, Deloitte and McKinsey & Company have singled out market segmentation and the development of holistic customer engagement methodologies as key strategies to raise revenue.

In her research paper 'Social Interaction via Social Media', Eileen Fischer argues that engaging with people on social media is not dissimilar to engaging with them in real life. It requires the establishment of a connection through common ground consisting of interest, values or beliefs. Many firms fall into the trap of seeking short-term gains without properly establishing connections. The significance of building connections and credibility amongst users is exemplified by the success story of JetBlue Airlines. The firm recently earned a 140% return on their social media investment. According to a report by Bain & Company, their success can be strongly linked to their real-time Twitter customer services, which were five times as efficient as their call centres. By directing investments towards improving customer experiences, JetBlue is now seen as a credible organisation with a clear conversion into high Net Promoter Scores and greater sales and revenue.

Another key aspect of successful social media campaigns undertaken by a range of firms is their homogenisation of target audiences. Bain & Company developed a consumer segmentation chart consisting of ten socio-demographic categories and their typical online habits. For example, 'mums' featured quite prominently in the 'social butterflies' category as individuals who heavily used personal networks and were predominantly young, working and female. In contrast, the groups 'bloggers' and 'social gamers' had markedly different roles and results. Computer firm Dell has enjoyed considerable levels of customer engagement through its social media channels by similarly identifying and targeting different groups with initiatives that appeal to them. For example, it engages 'Influencers', highly connected tech-savvy individuals, by helping them 'co-create' products through product-testing opportunities, online feedback forums and special recognition for their efforts.

The crux of an effective social media business strategy lies, however, in engaging with 'online communities'. This involves breaking down the traditional relationship gap between the buyer and the seller by engaging consumers in various organisational functions such as product development, operations, marketing, sales and customer services. McKinsey & Company estimated a collective annual growth in firms' aggregate value of between $900 million to $1.3 trillion when this is successful. Such engagement requires not only an expansion of a company’s agenda, but an entire
paradigm shift. The concept of an online community carries with it all the key traits we associate with a tangible physical community: social contracts, trust, collective engagement and an accepted community culture, practices and values. By promoting greater interpersonal engagement, firms and customers alike have the opportunity to collectively create, sell and buy products and services that they desire.

In conclusion, the treatment of consumers as homogenous entities, and an increasingly interpersonal engagement with them, promotes better relations between firms and their social media constituents. As these users become increasingly interconnected and interested in the activities of such organisations, social networks will likewise become increasingly interlinked and far-reaching in scope and business advantage. With the right strategy, social media engagement by businesses thus has the potential to spur not only stronger social communication and relationships, but moreover, stronger socioeconomic development and business revenues.

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Innovation, Global Finance and Fragility

Soumik Chowdhury

Most people would agree that the creation and addition of the ‘black box’ into carrier airplanes has helped our understanding of aircraft disasters and the strengthening of aeronautical safety. It is one example in a sea of many of the societal benefit that arises from innovation. However, this benefit does not hold true in the current global financial landscape – on the contrary, evidence suggests that financial innovation has increased market fragility. This article will examine the role that instruments of financial innovation played in exacerbating market fragility prior to and during the Global Financial Crisis of the late 2000s.

Financial Innovation: Definitions and Drivers

At its most basic, innovation is driven by the presence of a problem that acts as a potential fault in a structure. For example, the faulty structure could be a vehicle that at high speeds creates a risk of fatality for its driver; the innovation is the seatbelt that provides a safer environment at those same high speeds. Likewise, financial innovation is driven by perceived defects in the market, such as unfavourable taxation policy and the regulatory framework. However, unlike the seatbelt that increases safety, financial innovation has instead caused market fault lines to transform into large and visible fissures.

To understand why financial innovation is associated with increased market fragility, we must begin in a rudimentary fashion with the definition and drivers of financial innovation. According to Harvard’s Peter Tufano, financial innovation is the creation of new financial instruments and processes in order to meet the investment needs of large enterprises.¹

Since the 1990s, two major innovative instruments have emerged in global finance – Credit Default Swaps (CDS) and Collaterised Debt Obligations (CDO). CDS are classified as financial instruments in definition but actually resemble insurance policies in behaviour – they allow creditors (holders) to receive financial compensation if a particular economic event occurs, a common event being default.² Prior to the Great Recession, CDS reached $62.2 trillion in value but fell by over 50% by the end of the recession, highlighting the degree of market sensitivity between CDS and market value of assets.³
Collateralised Debt Obligations, meanwhile, involve large lenders (mostly well-capitalised investment banks) setting up separate entities which purchase and pool secure debt products such as mortgages and car loans into one security. They then slice that security into three compartments, or tranches, according to levels of risk tolerance and sell them to investors. Intrinsically, like CDS contracts, CDOs remain valuable if the market value of the collateral, i.e. mortgages, remains high and averse to the risk of default.

The process of securitisation in CDOs was designed to have a two-fold effect. The first was a financial effect – it would create the benefit of risk diversification, where investment banks could transfer the risk of holding various loans onto investors who could then select various risk profiles within that one asset. The second effect would be a macroeconomic effect of strengthening the supply of credit within the global economy. Furthermore, being a derivative, CDO product value was linked with the booming US housing market, which saw a large increase in the purchasing of property and the creation and value of mortgages.

Fast forward to the beginning of 2006 - investment banks were securitising CDO on one hand, and interacting with large-scale insurers to create CDS that protected holders against defaults on the other, and all the while the housing market kept rising. Following that final surge came one of largest falls in asset values in modern economics. Average property prices in the US deteriorated by more than 18% by the end of 2007 – the housing bubble had burst. Despite the consensus and justification for CDO and CDS as new financial products, a post-mortem examination of the Global Financial Crisis shows a fractured result.

Cracking Under the Strain

In analysing the role of financial instruments, we can focus in on one unarguable fact: financial products [CDO and CDS] and processes [securitisation] are inherently faulty when stress levels are stretched. This position of faulty securities suggests that when financial conditions are positive, the forecasts assigned to CDO and their cash flow generation are sound, but these lose validity when the economy is under financial stress. In order to create CDO securities, their originators identify, price and pool various secured debt instruments into a Special Purpose Entity (SPE). According to the Bank of International Settlements, an SPE is an off-balance sheet firm which buys and sells financial assets on behalf of its sponsor firm without having the sponsor firm place these assets on their own balance sheets. Typically, an SPE would purchase illiquid mortgages, transform them into CDO securities and sell these securities to investors after a particular turnaround time.

When the housing market collapsed, the turnaround time meant that SPE were exposed to an unsustainable level of risk within their portfolios, as they were left with unsellable mortgages whose prices were falling at an alarming rate. An empirical realisation of this inherent flaw in securitisation was the collapse of Lehman Brothers, a post-mortem of which revealed astronomical levels of bad debt via SPE. The perceived benefits of securitisation and the CDS insurance products resulted in the incentive to create and sell mortgages to banks, who then securitised and sold those mortgages for cash with which they purchased more mortgages to continue this cycle. The culminating effect was the housing bubble.

Adjacently, insurance firms such as AIG received billions of dollars in fees as the originators aimed to insure themselves against mortgage defaults by purchasing default swaps. When the
housing market crashed, the growing number of defaults within CDO portfolios activated the swap agreement, but these proved well beyond the financing capabilities of the insurance providers.12 The failure in honouring the CDS contracts instigated the panic that saw investors pulling their money out of various financial institutions and the share price of major banks plummeted from 2007 to 2008.13 The structure of CDS contracts and their synchronised relationship with CDO contracts and the housing market resulted in an extremely volatile financial product that mismanaged risk during boom times and led to large devaluations during bust periods.

The role of innovation in finance was to create new securities that generated a larger source of financing for corporations, businesses and individuals in order to sustain greater wealth generation and business growth. In reality, the results and the experience of the Global Financial Crisis show that this has not been the case. The 2000s have been a testament to the instability of the era’s financial innovation. To overcome this new fragile global economy that has emerged, firms and governments must re-evaluate the risk management instruments that are used in modern finance. It is the responsibility of regulators, creators, investors and financial engineers to ensure that the products being developed are carefully monitored, tested and retested to ensure that they remain robust in a highly dynamic global financial system.

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