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Developing Countries, Global Financial Governance, and the Group of Twenty

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Introduction to the G-20 Process

The Group of Twenty (G-20) will meet in Ottawa in mid-November, the third meeting since the group was created in 1999. In addition to the G-8 (G-7 plus Russia), the membership of the G-20 consists of: Argentina, Australia, Brazil, China, India, Korea, Mexico, Saudi Arabia, South Africa, Turkey and, oddly, two institutional representatives—one for the European Union and one for the Bretton Woods institutions (the IMF and World Bank).

The G-20 was unilaterally created by the G-7 at their Finance Ministers' meeting in September 1999. It was clearly intended and seen as the successor to the previous G-22, which had been hastily and unilaterally created by the U.S. in November 1997, in the wake of the Asian financial crisis of that year. (Its membership had included Hong Kong, Indonesia, Malaysia, Poland, Singapore, and Thailand, and excluded Saudi Arabia, Turkey, the EU and the IMF/World Bank; but was otherwise the same as that of the G-20.) G-7 sponsorship and Canadian chairmanship created marginally greater legitimacy for what was essentially the same U.S.-led effort to involve more countries in discussions—but not decisionmaking—relating to potential future systemic financial crises following the shocks of the Mexican, Asian, and Russian crises. There have been two ministerial meetings of the G-20 thus far: in Berlin in December 1999, and in Montreal in October 2000; both were preceded by Deputies' preparatory meetings. There is no secretariat nor does the G-20 have any working groups. Its materials and discussions are confidential.i

The creation of the Group of Twenty (G-20) by G-7 governments led by the United States in late 1999 represented a small step toward improved global governance in that it expanded discussion of some international financial issues beyond the bounds of the G-7, within which decisionmaking power continues to be closely held. But in terms of an appropriate process for global financial governance—one that is both legitimate and effective—I argue that the G-20 fails completely. Its creation totally ignored the serious and continued efforts of the developing countries, speaking collectively through their Group of 24 (G-24), to collaborate with the G-7 and other industrial countries in the creation of a more effective and legitimate process. The G-20 should therefore either be transformed substantially or closed down to permit the earliest possible "fresh start" of the effort to reform global financial governance.

Developing Country Context for G-20-Type Activity

Western academic and press accounts of the emergence of the G-20 describe it, without any historical context, as a U.S. or G-7 initiative. They virtually ignore the earlier, continuing efforts of the developing countries to interest the G-7 and other industrial countries in initiating a process of discussion of international financial governance issues that had at least some superficial similarities to the current G-20. (These efforts were well reported in the Southern News Service, SUNS, and the developing country press.) The differences between what the developing countries had suggested and what has emerged (in the form of the G-20) are great. Until they are more widely appreciated—and narrowed—there is little likelihood of appreciable progress in global financial governance.

FOREIGN POLICY IN FOCUS

The developing countries—all of them, not simply those of potential systemic significance—have been calling for serious dialogue with the industrial countries over international financial reforms, outside the constraining circumstances of the Bretton Woods institutions, at least from 1994 onwards. At that time, in connection with the celebration of the fiftieth anniversary of the Bretton Woods institutions, the G-24 conducted a highly constructive "technical" conference and set about its own institutional strengthening.ii

The subsequent G-24 Ministerial communiqué at the 1994 annual IMF/Bank meetings drew upon the findings of the conference. In response to the G-7's own call for an evaluation of the Bretton Woods institutions at their meeting in Naples in July 1994, the G-24 called for a fully representative intergovernmental process for such a review, drawing on the general model of the Committee of Twenty of the 1970s. Such a broad-based review would provide legitimacy, ensure ownership of the results, and be more effective than a narrow G-7 review. The G-24 Ministers agreed that the following topics should be included in the proposed review:

- the role that the IMF and the World Bank should play in ensuring that the management of economic policies is consistent with proper operation of the global economy;
- the working of the exchange rate system with a view to reducing exchange rate volatility and misalignments;
- the possibilities for enhancing the effective participation of developing countries in the decisionmaking process within the Bretton Woods institutions. In this context, the functioning of the Executive Boards of the IMF and the World Bank, as well as the role, functioning, and future of the Development Committee and the Interim Committee, should be examined;
- the appropriate modes of interaction between the Bretton Woods institutions and the regional financial and monetary institutions;
- the appropriate forms of interaction and division of labor between each of the Bretton Woods institutions and the World Trade Organization (WTO).

That request was reiterated in subsequent G-24 communiqués.

In 1995-96 the G-24 issued a paper outlining the way in which such a Review Group or Task Force might work, drawing on the most obviously relevant experience of the IMF's Committee of Twenty in 1972-74. It recommended the involvement of market practitioners, nongovernmental organizations (NGOs), and academics in the discussions and working groups supporting the group. At least four working groups were suggested, operating under a central secretariat that would convert group recommendations into proposals for intergovernmental decisionmaking. The suggested groups were to cover:

- international monetary issues, including the role of the SDR;
- management of capital flows;
- decisionmaking processes in the international financial institutions; and
- development finance.iii

At the same time, repeated informal representations were made by the G-24 to the G-7, both through official and unofficial channels, more particularly through the "sherpas" preparing for the annual G-7 Summit conferences, beginning with the Halifax Summit in 1995.iv Position papers on more narrowly defined issues were prepared by the G-24 for presentation to the "sherpas" and the summits in 1996 and 1997, in an effort to initiate some genuine dialogue at least at an official level. While there were sometimes encouraging "noises" among elements of G-7 officialdom, there was never any formal response.

Following the Asian crisis, an extraordinary G-24 Ministerial meeting in February 1998—attended by the Managing Director of the IMF, senior World Bank and UN officials, and many observer countries—drew up the "Caracas Declaration II." That document made the same recommendation (although altering the proposed terms of reference for a Task Force in response to the new circumstances). It read:

"The Group of Twenty-Four sees an urgent need for a wide-ranging review by a Task Force comprising industrial and developing countries of the following issues:

- the capacities and modalities of the international monetary and development finance institutions to respond in a timely and effective manner to crises induced by large-scale capital movements;
- the appropriateness of the conditions prescribed by these institutions to deal with such crises;
- the equitable sharing of the costs of post-crisis financial stabilization between private creditors, borrowers, and governments;
- the more effective surveillance of the policies of major industrialized countries affecting key international monetary and financial variables, including capital flows;

- the modalities for building domestic social safety-nets as integral elements of stabilization and adjustment programs to protect the most vulnerable elements of the population of crisis affected countries; and,
- the increased representation and participation of developing countries in the decisionmaking organs of the international community to properly reflect developing countries' growing influence in the world economy, including through the revision of the bases determining the voting power in international financial institutions."

By this time the U.S. had already initiated an effort to launch its own consultative process through the G-22. Until this unilateral U.S. action of 1997-98, issuing an invitation to twenty-one countries, of which ten could be described as "developing" (and who were scarcely in a position to protest about the processes of selection ... or anything else), there had been no response whatsoever to the developing countries' repeated representations. There has still been none.

Rescue of a G-20 Process?

Increased developing country representation in the key current discussions of international financial architecture and global monetary and financial reform, in the Financial Stability Forum (from 1998 onwards) and the Group of Twenty, is to be welcomed. These discussions, however, are so far primarily directed at the narrow question of the prevention and resolution of systemic financial crises, rather than the much wider range of reform issues in the financial system that require attention.

The G-20 is severely flawed in that it contains no representation either from the poorest and smallest developing countries, or from the European "like-minded" countries (the Nordics and Dutch) who, on the basis of prior experience, might be expected periodically to speak on their behalf. Presumably, this is because the poorest and smallest are unlikely ever to constitute any systemic threat. But there are major "architectural" issues surrounding the provision of adequate development finance to these countries and their peoples. They go well beyond the debates surrounding the "HIPC initiative"—which is the still wholly inadequate global response to low-income country debt servicing. In particular, the aid relationships of the past are no longer either functional or acceptable.

The rhetoric, if not yet the practice, of the aid donor community has already changed radically—in favor of more transparent and coordinated assistance in support of locally owned rather than under donor-driven programs, which are under the control of recipients not donors. Change in practices will eventually follow the change in rhetoric, however slowly it comes. Such reform could be accelerated by independent and much improved monitoring of donor performance at the country level, as well as continued monitoring of recipients.

Development finance and related issues are due to be addressed at the UN's high-level "event" in 2002 on "Finance for Development." But it is already clear that smaller, more focused, and less clumsy processes will be required—on an ongoing and continuous basis—if real progress in this sphere is to be achieved and sustained.

The G-20 does not possess mechanisms either for reporting or for accountability to the broader international community, such as the constituency system provides within the IMF and World Bank. Nor does it possess any provisions for transparency and nongovernmental inputs, both of which are required for its credibility and legitimacy, as well as its effectiveness.

The G-20's initial processes have been all wrong. Its origins in the G-7 reduce its legitimacy; its membership is not fully representative; its mandate is much too narrow; and its procedures lack provisions for nongovernmental participation, accountability, or transparency. As currently constituted, it is unlikely to lead anywhere. Its very existence deflects energies from more appropriate and hopeful processes and agendas.

There are four principal requisites for the possible rescue of the G-20 process:

1. It must alter its membership to improve its representativeness (while converting the IMF/World Bank from members to observers) and institute some sort of "constituency" system to ensure full reporting and a sense of ownership for non-members. The IMF/World Bank representatives should exercise leadership by resigning and, together with other UN agencies, pushing for such change;
2. It must declare its accountability jointly to the UN Secretary-General, the Managing Director of the IMF, and the President of the World Bank, with the expectation that its report(s) will be presented to the UN's Economic and Social Council and the two Executive Boards respectively, and to the forthcoming UN

Conference on Financing for Development;

3. It must make its discussion papers, documents, and reports publicly available, and encourage public and parliamentary debate thereon throughout the world; and include nongovernmental participation in its technical working groups or subcommittees;

4. It must significantly expand its agenda to address the full range of problems and issues in the international monetary and financial system, as addressed for instance in the UN Task Force Report on a "new international financial architecture," and establish technical working groups or subcommittees to address them all, as appropriate.v

The expanded agenda should include:

- provision of a more effective system for global macroeconomic management, including provision for adequate liquidity and emergency responses;
- a stable and equitable system of development finance for all developing countries and finance for development-related scientific research, especially in health and agriculture;
- an agreed framework of rules and obligations for international financial flows (including provision for prudential regulation of international financial markets and institutions), with a capacity for their effective and equitable application;
- increased representation and participation of developing countries at the decisionmaking level of international financial institutions to properly reflect developing countries' growing role in the world economy, including credible processes for the selection of chief executive officers and a more democratic allocation of voting power in these institutions; and
- most important of all, concrete provision of the financial requirements for the supply of the key elements of human development for all of the world's population.

None of these proposed "reforms" of the G-20 process are radical. As far as expansion of its agenda is concerned, there have already been suggestions from its chairman and others that this would be desirable. The other suggested changes seem obvious steps toward better governance and greater effectiveness.

If such a rescue of the G-20 cannot be carried out, it should be replaced. If it continues to exist, the G-20 should be complemented, as quickly as possible, by other, more appropriate institutions. Particularly if key governments are unwilling to participate, they should include wholly or partially nongovernmental ones.

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Endnotes

i For contrasting assessments of the early stages and potential of the G-20, see Roy Culpeper, "Systemic Reform at a Standstill: A Flock of 'Gs' in Search of Global Financial Stability," (Ottawa: North-South Institute, 2000), mimeo and John J. Kirton, 2001, "The G-20: Representativeness, Effectiveness and Leadership in Global Governance," in John Kirton, et al. (eds.) *Guiding Global Order: G-8 Governance in the Twenty-First Century* (Aldershot: Ashgate, 2001).

ii See UNCTAD, *International Monetary and Financial Issues for the 1990s*, Vol. IV, Special Issue, *International Monetary and Financial Issues: Developing Country Perspectives* (Geneva: UNCTAD, 1994) and Gerry K. Helleiner (ed.), *International Monetary and Financial Issues, Developing Country Perspectives* (New York: Macmillan, 1996).

iii Aziz Ali Mohammed, "Global Financial System Reform and the C-20 Process" in UNCTAD, *International Monetary and Financial Issues for the 1990s*, Vol. VII (Geneva: UNCTAD, 1996).

iv For details see Roy Culpeper and Caroline Pestieau (eds.), *Development and Global Governance* (Ottawa: IDRC and North-South Institute, 1996).

v For the UN Task Force see, United Nations Task Force (of the Executive Committee of Economic and Social Affairs), 1999, *Towards a New International Financial Architecture* (CEPAL, Santiago). See also, José Antonio Ocampo, "International Financial Reform: the Broad Agenda," *CEPAL Review*, 69, December 1999.