The G20 & Global Governance

By Sachin Chaturvedi & Priyadarshi Dash

Author Sachin Chaturvedi *Author Priyadarshi Dash*

Introduction

A diverse set of "movers and shakers" have explained the contours of global governance over the past decade. Some important developments that need mentioning in this parlance include the collapse of the WTO Doha Round of trade negotiations, the origination of the financial crisis of 2008-2009 in the United States (the most sophisticated financial system in the world), the unhealthy trade war between the US and China, the so-called proponents of free trade, protectionist and isolationist policies in the US, migration from conflict-ridden Arab countries and Africa, and human rights violations across countries. These unusual events happening across countries regardless of their level of development tempts the intelligentsia and ordinary citizens to question the relevance, adequacy and legitimacy of the existing superstructure of global governance. Moreover, the slow response to standard bailout and crisis financing packages by the IMF in the wake of the financial crisis in 2008-2009 and the prolonged and uncertain recovery have exposed inherent deficiencies in the current systems of global governance.

The post-crisis evolution of narratives on the role of multilateral institutions and country configurations or reconfigurations has been kaleidoscopic and introspective. While pressure on the institutions of global governance such as the United Nations, IMF, WTO, World Bank and regional development banks to undertake necessary reforms in their functioning, particularly on the issue of fair representation of emerging markets and developing countries, continues to mount, there is a greater recognition of the existence of a vacuum in international economic governance. Can the G20 fill this vacuum? In other words, can the G20 demystify and blur the conventional country configurations into stereotype categories of developed and developing, and nurture mutually-reinforcing engagement among countries?

Despite not having the legal status of an international organization, the G20 has gained substantial influence as a global platform in recent years, perhaps by leveraging the benefit of the doubt. This benefit of the doubt accrues from declining faith in the existing multilateral processes of promoting trade, investment and development cooperation. In the 1980s, the G7 lost its importance as a platform for international economic policy coordination and this skepticism lasted till the outbreak of the East Asian Financial Crisis in 1997. The severity of this emerging markets crisis in terms of contagious spread and magnitude of output and employment loss created the space for the G20 to emerge ("G20 and Global Governance" by Stephen Kirchner, *Cato Journal*, 2016, Vol. 36, No. 3). Subsequently, the first meeting of the G20 finance ministers and central banks was held in Berlin in December 1999. Regardless of the efficacy of other country groupings, the expectations from the G20 appear to be high as the grouping has graduated from playing a stabilizing role (in the context of post-crisis inter-country coordination) to promoting development. This has been manifested in the widening and broadening of the G20 Summit agenda from its focus on restoring financial stability and ensuring global macroeconomic coordination in the first three G20 summits during 2008-2010 to a wide range of development issues like global value chains, food security, skill development, women empowerment, Africa compact, and so on. Being a club of developed as well as emerging markets, the G20 envisages a world that cherishes high and inclusive economic growth, protects the interests of the poor and marginalized, prevents financial crises, and ensures upward social mobility (poverty alleviation, food security, women empowerment, etc).

Basically, the business of the G20 over the years has evolved in two tracks – a finance track and a development track. Even though the leaders' summits have not exclusively referred to these two tracks for practical purposes, they define the sequence of activities in the G20 platform. As this year's G20 host, Japan has cautiously identified the core areas of these tracks. In development sectors, universal health coverage, aging, and quality infrastructure assume importance, while the finance track will probably continue to implement regulatory reforms in financial markets and envision new and innovative means of fund mobilization for development projects.

Finance Track

As the name suggests, the finance track largely covers the areas of global financial stability, fiscal and monetary policy coordination, exchange rate coordination, financial systems development, and development finance issues. The success of G20 initiatives in restoring financial stability to the global economy is laudable. However, a lot depends on the measures and commitments beyond crisis prevention and resolution. The vitality of the finance track can only be regarded as successful if finance contributes to inclusive and sustainable development in emerging and developing economies.

Functioning of Global Financial Systems

The G20 assumed prominence during the global financial crisis of 2008-2009 when it facilitated joint efforts by the advanced economies and emerging markets to restore financial stability and ensure a coordinated macroeconomic response, and resist resorting to beggar-thy-neighbor policies. The smooth and coordinated implementation of fiscal stimulus packages and adherence to monetary policy and exchange rate disciplines helped contain the crisis-related disruptions in the affected economies. These issues dominated the commitments of the G20 at the first three summits. While short-term crisis prevention and mitigation continued to occupy substantial attention in subsequent summits, the finance track of the G20 has widened significantly in terms of issues covered and the scope of commitments. A good number of commitments refer to long-term structural reforms, especially reform of international financial institutions, the expanded mandate of the Financial Stability Board (FSB), mobilizing private capital for infrastructure financing, promoting institutional and long-term finance for development, measures to address debt sustainability, and tax and accounting reforms.

In October 2018, the G20 Eminent Persons Group (EPG) submitted a report on the global financial system. The EPG was tasked with a mandate "to recommend reforms to the global financial architecture and governance of the system of International Financial Institutions (IFIs), so as to promote economic stability and sustainable growth in a new global era; and to consider how the G20 could better provide continued leadership and support for these goals" (G20 Secretariat, "Making the Global Financial System Work for All, Report of the G20 Eminent Persons Group on Global Financial Governance"). Unfortunately, most of the proposals of the EPG do not reflect this central mandate. On the contrary, the report reiterates continuation of certain practices which have long been the subject of criticism. A number of EPG recommendations seek for the G20 to allow the IFIs to lead harmonization of regulations, standardization of risk assessment and mitigation, mobilization of capital for infrastructure and development financing, and attracting private capital. There are many contentious issues in the provision of and access to global governance, especially in the economic and finance domain. Developing, less developed, small and vulnerable economies would ideally demand more space for representation in global affairs than remaining dependent on their fortunate large and developed economy peers.

In order to realize the full potential of a cooperative international order, it is important that developing countries are given fair and democratic representation in the decision making of IFIs, particularly the IMF and the World Bank. Despite repeated efforts by developing countries including India for action on long-pending reforms of the IMF and World Bank, not much has happened except some revision in the IMF quota formula and inclusion of the Chinese currency, the renminbi, in special drawing rights. As it appears, taking forward the EPG proposals in any manner would amount to empowering the IFIs, and contribute to perpetuation of existing inequities. It could also erode the policy-making space of the sovereign nations. Moreover, the proposals sound self-defeating as they would re-establish the flawed pre-eminence of the IMF in global macroeconomic governance. It is an over-optimistic claim that governance and human capital development have been at the core of the IFI's operations. Among IFIs, the IMF has supported countries during balance of payments crises as the lender of last resort but with conditionalities and Structural Adjustment Programs (SAPs). The efficacy of SAPs for developing countries implemented in the past has been mixed, especially taking into account the experience of small developing economies and Least Developed Countries (LDCs). The G20 should work to suggest and commit to reforms that bring inclusive development, not packaging old wine in new bottles.

The idea of country platforms or any kind of joint platform within the G20 is indicative of an unhealthy trend of cartelization among the IFIs. Without country platforms the G20 can unlock investments in the member countries. Creating an enabling environment for attracting investment should be left to the member states rather than the G20 as a whole. The G20 should enable countries to explore various sources of financing for development. Instead of the G20 creating any such platforms, IFIs can pool their own resources in a common platform without making countries party to that arrangement, and offer them development finance, if approached by any country. By that logic, regional platforms for promoting cross-border investments and connectivity are also not required. Regional platforms would have to necessarily align themselves with the priorities of the member countries in regional cooperative frameworks, like Bangladesh, Bhutan, India and Nepal (BBIN), the Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation (BIMSTEC), etc.

In practice, the IFI community has placed excessive emphasis on promoting financial liberalization in developing countries. So far, this paradigm has not led to holistic social and economic development in

the developing world. The pitfalls of such an approach were anticipated by Gunnar Myrdal long ago. Myrdal, in three volumes of *Asian Drama: An Inquiry Into the Poverty of Nations* and other works, underscored the importance of making a fine balance between a *laissez-faire* economy and state intervention. For example, Brazil had a very active stock market which virtually disappeared following liberalization that allowed local companies to be listed on the New York Stock Exchange. The EPG also argues for convergence of early warning systems, which is a no brainer. Early warning systems have not been effective in predicting financial crises in the past. Although there is a need for continuous surveillance and assessment of risk build-up, it is more efficient to have independent systems of macro-economic risk assessment by institutions such as the IMF, FSB and the Bank for International Settlements than the integrated system. It will help maintain the plurality of early assessment systems as well as contribute and validate the predictive ability of the alternative models. IFIs have failed in anticipating the occurrence of financial crises in Asia and Latin America in the past and most importantly in the United States and the Southern European countries in recent years. Moreover, the post-crisis policy prescriptions offered by the IMF and other IFIs to the crisis-affected economies proved counterproductive and resulted in unwanted economic adjustments. Interestingly, in the early years of these institutions, Harry Dexter White and John Maynard Keynes, eminent economists in this field, were apprehensive of the role and contribution of the IMF and World Bank in pursuit of growth and full employment.

The idea of reorienting development finance by involving the non-G20 constituencies and the IFIs appears to be an unnecessary step. This is an attempt to legitimise the leadership and intervention of the IFIs in G20 matters. This could be a barrier to developing country institutions such as the New Development Bank and the Asian Infrastructure Investment Bank in developing their own procedures. The G20 is not a legitimate global platform; therefore it would be a futile exercise for the G20 to take the responsibility of reorienting development finance by involving IFIs and non-G20 constituencies as it may not be acceptable to the global community. After all, at the meeting in Busan, the developed countries had attempted harmonization of approaches to aid which was rejected by the developing countries.

The report is misleading as it apparently assigns more weight to preventing short-term financial crises as an indicator of healthy development compared to the role of other important development parameters. The IMF is mandated to primarily provide short-term balance of payments financing. The idea of combined assessment of development risks recognizes the undue emphasis on crisis prediction and management, which is unnecessary at this stage of the evolution of the G20. Financial stability and macroeconomic coordination were the over-riding objectives of the G20 in the immediate years following the financial crisis in 2008-2009. Since then then G20's agenda has expanded to include various development issues. Now that the global economy is seeing buoyancy after a prolonged slowdown following the financial crisis, the G20 should prioritize expeditious implementation of its commitments on various development goals.

Leveraging on Private Capital

Private capital, especially cross-border capital flows, has not been efficiently harnessed by developing countries. This pattern more or less holds across all regions, although there are slight differences. Most countries have relied on official aid flows and concessional funding which would not suffice given the extent of development gaps in developing Asia and Africa. Developing countries in Asia, Africa and Latin America need massive investment in physical and social infrastructure in the next 20 to 30 years. It would not only require efficiency in existing resource use but identifying new and innovative sources of funding, with significantly large contributions of private capital. Paradoxically, globalization has inverted traditional economic views of the desired direction of international capital flows. Rather than encouraging capital to flow to places where it is scarce, globally-mobile capital flows to places where it is most secure. This pattern is creating distortions in the efficiency and equity of investment around the world, especially of government investment.

While public investment would remain a vital component of development finance, the G20 should take proactive steps now to promote a more efficient allocation of private capital through new forms of public-private partnerships. A unified ecosystem, good governance and investment in human capital would attract private capital into desired sectors of investment. Blended finance and local currency financing facilities are novel supplementary financing windows. Small and medium enterprise (SME) financing and agribusiness have been dynamic sectors. Private financing in low-income countries and fragile states is feasible as healthy mobilization ratios (total cost of investment per unit of IDA resources) of 8:1 have been realized (International Development Association. *IDA18 IFC-*

MIGA Private Sector Window (PSW): IDA18 Mid-Term Review. 2018).

The G20 should promote long-term institutional capital from G20 countries into investments related to the Sustainable Development Goals (SDGs). Some countries face particular issues, especially low-income countries, fragile states and selected LDCs. For example, there are 12 LDCs that will graduate from this group in the next few years with consequent loss of duty-free, quota-free preferential market access and aid for trade under the WTO window. They may need special attention for financing to manage their current account deficits during this transition. A balance is needed between macro, micro and affordability/access concerns that should be based on detailed country considerations. Rules of thumb are not good proxies in these debates.

Financing Global Public Goods

Global public goods cannot be created with pure commercial terms of funding. There is a need for special or dedicated funds. International collective action is warranted to fund non-rival and non-excludable functions like research and knowledge sharing, control of pandemics and mitigation of global warming, and global standard setting, visioning, convening and advocacy on policies, such as the Food and Agricultural Organization's principles for responsible investment in food and agriculture ("We Need a Consensus on the Definition of 'Global Public Goods for Health'," by Gavin Yamey, Osondu Ogbuoji and Kaci Kennedy McDade, *Brookings Future Development*, Nov. 20, 2018). G20 members constitute the largest economies in the world and hence will be the main contributors to these potential funds. They should negotiate on such funds. They could learn from the experience of the UN in its new Funding Compact which strives to rectify the imbalance between stagnant core contributions and rising non-core, voluntary contributions that have to be continuously renegotiated. Wise use of new innovative sources of funding would be a pragmatic step in this endeavor.

Development Track

Unlike the finance track, the development track or the Sherpa track covers a whole range of sectors and issues which have larger development implications. To name a few, food security, economic empowerment of women, agriculture, and skill development have significant bearings on the lives and livelihood choices of the poor and excluded sections of the people. In the last 20 years, and particularly since 2008, the G20 agenda has had commitments on various development issues. Some areas that could be potential game changers in the development track are discussed below.

Science, Technology and Innovation (STI) for Meeting SDGs

Technology development, deployment, dissemination and transfer to developing countries require suitable responses. Current institutional arrangements are not equipped to meet the genuine needs of developing countries in technology development and transfer. The UN has undertaken several initiatives over the years in the area of technology transfer, including 1) the Multilateral Fund under the Montreal Protocol; 2) the Green Climate Fund, 3) the Global Environment Facility (GEF); and 4) the Climate Technology Centre and Network of the United Nations Framework Convention on Climate Change (UNFCCC). These are necessary and are not sufficient as more is needed in terms of research and development, funding, technology transfer and adoption and in terms of synergy among them. The 2030 Agenda, *prima facie*, has only produced a rough skeleton of the proposed Technology Facilitation Mechanism (TFM). Mapping of capacity gaps in developing countries for technology assessment, particularly in the domains of development and sustainability in tune with the SDGs should be undertaken. Proper ecosystems with specific (cost-effective) technology solutions should come up in individual countries and contribute to the global repository. A universal technology bank should be created as the core institution of the TFM. The activities around a TFM technology bank and dissemination of technologies require careful policy design to mitigate informational asymmetries and address market failures and other systemic challenges.

Novel models for incentivizing innovation, such as open source, open innovation, crowd sourcing and innovation prizes, can be explored and adopted. In this regard, the literature on successful examples and models and their adoption in different sectors, ranging from agriculture to drug discovery, is growing. Addressing technology-related issues from a public goods perspective will enable finding workable solutions. Global public goods can be produced and adopted to find cures for communicable diseases, enhance productivity in agriculture, protect environmental commons, and enable access to information and knowledge. Successful examples of such cooperation include the Consultative Group on International Agriculture and the European Organization for Nuclear Research. Further, integrating the SDGs in STI cooperation has not happened

and there is a disconnect between STI cooperation and strategies for the SDGs. There is a strong case to use STI cooperation to meet the SDGs by developing specific programs and mechanisms. The current frameworks and agreements in STI cooperation can be analyzed from an SDG perspective, and institutions that facilitate STI cooperation can be asked to integrate relevant SDG targets as an objective for STI cooperation.

Global Value Chains

As production fragmentation intensifies globally, countries can benefit from integrating into global value chains (GVCs). Currently, trade flows and positioning in GVCs in Sub-Saharan Africa are far below their potential. Lower tariffs, better access to credit for the private sector and a conducive business climate can enable better integration of Sub-Saharan countries into GVCs. Since the G20 already has the Africa Compact initiative, GVCs may strengthen the export prospects of African countries. The same would apply to developing economies in Asia and Latin America as well. Trade facilitation in the form of modern customs and border procedures have the potential to facilitate efficient integration of African economies into GVCs as trade flows in intermediate products are more sensitive to trade facilitation changes. As wages rise in East Asia, production can be pushed to relatively low-wage areas, possibly Africa. However, Africa can only tap this opportunity provided appropriate policies are in place for developing requisite skills among the local workforce, as well as investment in institutional reforms, particularly in technical education and training. At the same time, liberal foreign direct investment regimes may attract investment into industrial sectors in Africa which would fuel local industrialization and strengthen participation in GVCs.

Trade Finance

Globally, one-third of international trade is backed by one or two trade finance instruments. By providing financial support and insurance for uncertainty in payments by importers and delays in meeting orders, trade finance instruments support the trading firms. In Africa, trade finance is a relatively low-risk portfolio for commercial banks. The overall default rate is 5% whereas SMEs face the risk of a 14% default rate. Better provision of trade finance would help integrate SMEs into the mainstream economy and expand their capacity to export. Lack of adequate collateral and poor creditworthiness often leads to rejection of applications by the banks. Development banks like the African Development Bank and African Export-Import Bank could fill this perverse gap in trade financing and activate the hidden triggers for export growth in African economies. The G20 should enable adequate provision of trade finance to developing countries so as to enable them to benefit from trade liberalization, particularly from GVCs.

Conclusion

Good global governance is a *sine qua non* for achieving sustainable and equitable development in the world. The G20 has to play a critical role in this endeavor. Since countries have already embarked upon achievement of SDGs, the G20 must envisage and steer effective inter-country cooperation mechanisms for realization of this goal. Too much dependence on the IMF, World Bank and other IFIs would not help. In other words, the G20 relegating responsibility to IFIs using their own platforms would not serve the purpose. In fact, IFIs should undertake reforms of their organizations on their own. The finance track must keep the onus on reforming the Bretton Woods institutions and other institutions of global governance.

Global governance is not just about providing finance but putting in place institutional mechanisms that adequately address the vulnerabilities of countries in the long run. Private capital must supplement public investments in infrastructure development and other critical areas of social infrastructure. Cooperation in STI will be an important pillar in developing partnerships in the future. The G20 must nurture such partnerships which would not only help achieve SDGs but provide indigenous technological solutions to numerous development problems. GVCs offer vast opportunities for developing countries to benefit from integration with the rest of the world. Trade facilitation and financing would enable the countries to expand exports and create millions of jobs. With respect to contributions to global governance, the G20 should assign topmost priority to attainment of inclusive and sustainable development and promote global institutional architecture for minimizing country vulnerabilities. In that endeavor, the G20 should proactively advocate for necessary reforms in the existing institutions of governance and adhere to the spirit of mutually beneficial international cooperation. JS

Sachin Chaturvedi and Priyadarshi Dash are director general and assistant professor respectively at the Research and Information System for Developing Countries (RIS), a New Delhi-based think-tank.