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Section 1
Introduction

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1 The G20: Evolution, Functioning and Prospects

A Concise Review

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Introduction

Global economic governance, both policy coordination and international regulation, from the 1960s was organized by small networks outside the formal global governance institutions. It was, in effect, a 'minilateralism'[2] of a dominant few that used soft law as well as a loose coordination mechanism characterized by rules voluntarily agreed and monitoring and enforcement to achieve desirable results. The group of a handful provided the political critical mass for addressing the most urgent needs of the global economy and imparting a sense of urgency in the global governance agencies that had the formal mandate to tackle such issues. Informality and flexibility were central to the success of the arrangements.[3] The G7 was one such dominant network in the latter part of the twentieth century.

The balance of global economic power in terms of GDP and international trade in the early 2000s had become more dispersed, with a need for recognition of this new balance. The formal Bretton Woods system, its mandate, and mode of operation had become somewhat wanting in this new world order of the 2000s. Its inability to recognize or expand the role of emerging economies meant that they could not cope with changing times. Even the dominant triad of the G7 – United States, Japan and Europe – could not adequately counter interconnected challenges including macroeconomic imbalances, development imbalances or the provision of global public goods, in particular, energy, commodities and environmental sustainability.

Emerging economies, with superior growth performance in recent years, increasingly began calling for a place at the negotiating table. The Asian economic crisis of 1997–98 and the global crisis of 2008–09 finally resulted in modifications in the way global economic governance was organized. The formal governance system – the UN Security Council, the International

Monetary Fund (IMF) and the World Bank – were not adequately suited for resolving emerging crises as they primarily reflected the preference of the old world order, hence were increasingly unable to enjoy the confidence of the emerging economic powers. The need of the hour was a truly global network that adequately reflected the new political and economic multipolarity, and to synthesize a more representative balance of power with a transparent framework for global economic governance. Thus was born the G20 Finance Ministers and Central Bank Governors' Network in 1999 after the Asian crisis and the G20 at the Leaders' level in 2008 with the onset of the global crisis.The emergence of the G20 recognizes the fact that, in an increasingly integrated world economy, problems become, more often than not, global. This, in turn, demands global solutions involving all stakeholders, including the newly emerging market economies.

This chapter attempts to succinctly explore the origin and development of the G20, the evolution of its agenda, its relations with formal multilateral institutions, its performance and the future outlook for the group.

G-x: Purpose, Evolution and Shortcomings

Informal groups (G-x) emerged as a result of changing global scenarios especially when formal coordination mechanisms lagged behind or failed. In the 1970s, following the collapse of the Bretton Woods exchange rate arrangements, together with twin oil crises and subsequent stagflation in the global economy, formal mechanisms were too slow to conjure up quick solutions. Emergence of the G-x (G10/G7/G8)[4] functioned as an effective mechanism for the handful of advanced economies to cope with new challenges.

The aim of these informal mini-lateral processes, in the context of complex global economic interactions, has been to provide political and strategic leadership and, in the process, function as the inner core of a more formal multilateral process, i.e., the Bretton Woods system. The G-x provides an informal vision, a sense of direction and a political stance for needed actions to the formal decision-making bodies. In the late 1970s, the G7 emerged as such a platform for coordinating macroeconomic policies among advanced industrial countries, setting international standards, e.g., Financial Stability Forum (FSF), and promoting international trade and development aid. It further expanded to include non-core issues such as environment, energy, food security and terrorism (Alexandroff, 2010).[5]

As the G7 expanded to include Russia to become G8, it became the global steering committee through the 1990s when a series of market crises hit the global economy. After the crises, it was clear that the global steering committee that did not include systemically significant developing countries would be inadequate for future crisis resolution or prevention. There was a need for a wider outreach to include emerging economies. Hence, in 1999, an informal network of finance ministers and central bank governors for 20 countries (G20) was established.

G20 Finance Ministers and Central Bank Governors' Network

The first G20 communiqué noted that the purpose of the network was to create a platform for informal dialogue on economic and financial issues to encourage cooperation among systemically important advanced as well as emerging economies to achieve stable and sustainable global economic growth.[6] The initial mandate reflected crisis prevention as the central objective. However, the G20 increasingly expanded its agenda to include combating the challenges of globalization for emerging economies, curbing terror financing in the aftermath of the 9/11 terrorist attack on the World Trade Centre in New York City and ensuring the effectiveness of development aid, in addition to the development of domestic financial markets, regional economic integration and resource security (Group of 20, 2008).[7]

As indicated in its first communiqué that the G20 would dialogue 'within the framework of the Bretton Woods institutional system',[8] the heads of Bretton Woods institutions, i.e., the Managing Director of the IMF, the President of the World Bank and the Chairpersons of the International Monetary and Financial Committee and Development Committee of the IMF and World Bank, were granted ex-officio status to participate in the discussions.

Selecting the countries was informal. Though economic weight was argued to be the guiding principle, the size of the economy, neither in terms of absolute size nor in terms of Purchasing Power Parity (PPP) calculations could be easily translated to the inclusion in G20 membership. Apparently, other factors such as countries' systemic importance measured in terms of their global integration, ability to contribute to global governance and fair geographical representation played a significant role (Jokela, 2011).[9] Factors such as political stability and ideological proximity were also apparently considered, with some observers reasoning that the G20 was a mere 'reflex of the G7 world' (Wade, 2009). Wade stated that:

> [G20 countries] were selected by Timothy Geithner at the US Treasury in a transatlantic telephone call with his counterpart at the German Finance Ministry, Caio Koch-Weser. Geithner and Koch-Weser went down the list of countries saying, Canada in, Spain out, South Africa in, Nigeria and Egypt out, and so on; they sent their list to the other G7 finance ministries; and the invitations to the first meeting went out.[10] (p. 553)[11]

Be that as it may, apart from the inclusion of systemically important emerging economies in the global governance process, which was a watershed moment in itself, the G20 in its initial years enjoyed moderate success in building consensus on global financial matters. These included understanding on setting standards and codes to enhance transparency in the global financial system, introducing a framework for debt restructuring and initiating reforms at the Bretton Woods institutions, especially quota and representation reforms. In the early 2000s when the Asian market crisis was already behind, the initial impetus of G20 was lost as there were no new major non-G7 agenda, and quota and representation reforms were close to an impasse.

The critics argued that, even in its initial phase, the G20 had stayed under the shadow of its senior cousin, the G7. The G20 communiqués closely followed the communiqués of the G7 and, if there were any conflict, the G7 preferences prevailed (Martinez-Diaz and Woods, 2009; Martinez-Diaz and Woods, 2010).[12] In another study, Martinez-Diaz (2007), taking G24[13] communiqués as representative views of non-G7 countries, showed that the G20 communiqués were dominated by the G7 preferences and that non-G7 countries in G20 were silent and neutral.[14] Further, some critics argued that the existence of the G20 nipped any radical alternatives to be undertaken by the emerging markets. For example, major emerging economies, such as China and India, were cautious in G20 meetings. Thus, a perusal of the literature reveals that there has been a significant number of detractors to the G20 process.

G20 at Leaders' Level: Changing Political Climate

The decade following the inception of the G20 witnessed drastic geopolitical changes, increasing global interconnectedness and new growth poles. It was increasingly difficult for the G7, whose economic weight declined relatively, to provide global governance without effectively involving major emerging powers. Calling on the G20 to replace or fill in the shoes of the G7 was not straightforward. A G8 outreach programme, the Heiligendamm process, was initiated in 2007 at a G8 summit in Heiligendamm, Germany. The new G8

+ 5 included Brazil, China, India, Mexico and South Africa. However, the outreach programme was criticized by emerging economies as their inputs were not sought. The Indian Prime Minister Dr Manmohan Singh expressed his apprehension as,

> [T]he expanded group (*G-8 + China, India, Brazil, Mexico and South Africa*) is not cohesive since the countries included for purposes of outreach do not participate fully in the proceedings, or the preparations, and the expanded group therefore does not have a composite identity. Second, these groupings do not have any special legitimacy within the UN System.[15]

The report of a High-Level Panel on threats, challenges and change constituted by the United Nations stated that,

> While the annual meetings of the G8 group at a head of state or government level fulfill some of the characteristics required to give greater coherence and impetus to the necessary policies, it would be helpful to have a larger forum bringing together the heads of the major developed and developing countries. One way of moving forward may be to transform it into a leader's group – the G20 group of finance ministers, which currently brings together States collectively encompassing 80 per cent of the world's population and 90 per cent of its economic activity, with regular attendance by the International Monetary Fund, World Bank, WTO and the European Union.[16] (p. 88)

As the global economic crisis escalated in 2008, the need for involving emerging economies to effect meaningful coordinated solutions and impart confidence in the markets was met through the G20's representative power and legitimacy achieved through its high proportion in global GDP, trade and finance.

If the 1997 Asian crisis highlighted the extent of financial integration of emerging market economies and the need, through global dialogue, to take their views, the 2008 global crisis exposed the inadequacies of the existing formal global governance arrangements and the inevitability of a more pronounced role of emerging economies in structuring frameworks for solving global problems. The newly emerging geopolitical scenario culminated in designating 'the G-20 as the premier forum' for international economic cooperation at its Pittsburg Summit.[17]

Martinez-Diaz and Woods (2009) argued that emerging economies have also used their experience with the G20 summitry to accumulate institutional knowledge of the G-x process. They built up capacity at their respective ministries – usually finance and external affairs – to deal with G20 issues. They indicate that, 'ten years of practice in the G20 finance network means that the emerging economies have come into the G20 Leaders' network much better prepared for global summitry than they were in 1999.

G20 Agenda and Concerns

When the G20 Leaders' first Summit was convened, the need of the hour was to restore the confidence in the global financial system which was at the root of the global crisis. In the Washington Summit held on 14–15 November 2008, a 47-point action plan was agreed upon to identify the vulnerabilities exposed by the crisis and to improve regulation to adequately strengthen the financial sector. The Leaders also agreed to resist any protectionist tendencies. By the second Leaders' Summit held in London on 2 April 2009, a global recession had set in. The Leaders agreed on coordinated fiscal and monetary stimulus measures to check the recession and recapitalize the international financial institutions (IFIs) and multilateral development banks (MDBs) to assist developing countries cope with the crisis. Financial sector regulation was taken up by expanding the erstwhile FSF to include the dynamic emerging markets in the Financial Stability Board (FSB). It was mandated to coordinate financial sector regulation initiatives along with the IMF and Bank of International Settlements (BIS).

The Pittsburgh Summit held on 24–25 September 2009, marked the watershed moment in the G-summitry initiatives for global governance as Leaders designated the G20 as the premier forum for international economic coordination. The G20 expanded its agenda by laying out the 'Framework for Strong, Sustainable and Balanced Growth' to coordinate global recovery by reducing global imbalances. Voice and representation reforms at IMF to adequately reflect the new world order was assured. Financial sector regulation initiatives progressed further as measures to identify and regulate systemically important financial institutions (SIFIs) were endorsed. The Toronto Summit on 26–27 June 2010 further consolidated the initiatives of previous summits.

The Seoul Summit, the first Leaders' Summit chaired by a non-G7 country on 11–12 November 2010, delivered on many of the commitments previously made and initiated a whole set of new agenda and items to include the concerns of emerging and developing countries. Basel III norms proposed by the Basel Committee on Banking Supervision (BCBS) were endorsed. Transferring 5 per cent IMF quotas to dynamic emerging economies from over-represented countries was agreed upon. The IMF introduced two new lines of credit for the enhancement of global financial safety nets, a Flexible Credit Line (FCL) and a Precautionary Credit Line (PCL). Constructive steps were initiated under the Framework for Strong, Sustainable and Balanced Growth, as Leaders agreed to develop guidelines to measure and devise solutions to check destabilizing movements in indicators. Embarking on a new path, Leaders also endorsed the Seoul Development Consensus for Shared Growth. This is explained in the next section.

Expanding the Agenda: Development Consensus

The initial Leaders' summits were dominated by issues such as policy coordination to ward off impending recession. They put in place meaningful financial sector regulation and attempted to reorient the global economy towards reducing global imbalances, a rather G8-like agenda. However, those were the need of the hour to quickly restore confidence in the global economy. With the backdrop of coordinated stimulus packages, the global economy fared better than expected in 2009 and recovered well in 2010 (WEO, 2010).[18] It was felt that time was ripe for the G20 to transform itself into a global steering committee rather than a limited crisis containment group and look beyond macroeconomic and financial sector issues.

Many emerging economies expressed the need for expanding and reorienting the agenda to include developmental issues that are intrinsic to traditional macroeconomic factors (Shome and Rathinam, 2011).[19] As emerging economies were expected to contribute to global growth, introducing a development agenda would have been complementary to existing G20 objectives, especially for 'strong, sustainable and balanced global growth'. A strong development agenda in the form of global cooperation for investment in infrastructure, food security, freer international trade and human resource development was perceived to be integral to boosting the growth performance of emerging and developing countries. It was also felt that the formal multilateral arrangements lacked impetus in dealing with these crucial issues. Instead, the G20 was well placed to provide the political momentum to achieve these goals.

The South Korean G20 presidency, seeing itself as a bridge between the G7 economies and the emerging world, steered the G20 agenda towards development goals. Strongly backed by the emerging economies, a comprehensive framework for a 'Development Consensus for Shared Growth' was agreed at the Seoul Summit. It must be admitted, however, that some detractors believed there was a certain measure of incrementalism as the early financial stability focus of the G20 moved on to include additional objectives. Shome (2011)[20] pointed out that the nine pillars of development that emerged

> …challenged the singular focus that is needed to address the most crucial faultlines that should be addressed for restoring stability in financial flows. The lesson is that, in the prevailing era, the widely accepted concerns of global governance appear to embrace so many aspects and issues that they compete with the central issues that demand singular attention for achieving systemic correction. The broadening of objectives assuages the developing countries that claim recognition of their long-term structural concerns as a group. However, it carries the danger, and perhaps the reality, of diluting the immediacy of instituting strong and meaningful global indicators that should automatically trigger tightening/loosening macroeconomic–financial and fiscal–policies that most advanced economies should be implementing now. (pp. 94–95)

India is one of the active supporters of a development agenda for both bringing in new items on board as well as reorienting the focus of existing concerns to address issues of development. The Indian Prime Minister, for example, stated that channelling global savings into infrastructure investment in emerging economies will 'not only address the immediate demand imbalance, it will also help to address developmental imbalances'[21] by stimulating domestic demand and imports in emerging economies. This will not only lead to faster growth in emerging economies but also to a speedy global recovery. China also backed the development agenda to 'narrow the development gap and promote common growth' and 'further unleash the development potential of emerging markets and developing countries, and boost the economic growth of developing countries in order to stimulate aggregate global demand.'[22]

The G20 Leaders in Seoul in November 2010 set up a high-level panel on infrastructure investment with recommendations for 'financing infrastructure needs, including from public, semi-public and private sector sources, and identify, with multilateral development banks, a list of concrete regional initiatives'.[23] The panel recommended the G20 to build local capability especially PPP units to prepare bankable projects, an effective enabling environment for the model to work and ways for MDBs to effectively support the development of PPPs.

The latest Summit at Cannes on 3–4 November 2011, was however,