The G-20: Development and the Role of Developing Countries

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Introduction: Development on the Agenda

The G-20 leaders agreed at Pittsburgh last year on a framework for strong, sustainable and balanced growth. The leaders' meeting in Toronto in June of this year concluded that their monetary and fiscal actions had stemmed the crisis and the world economy was beginning to recover. Furthermore, they were engaged in regulatory reform of the global financial system. The leaders began to tackle longer-term issues and set up a Development Policy Working Group. The working group is to draw up a plan for action for discussion by the G-20 leaders in Seoul followed by discussion of its implementation in France in 2011. The agenda for the Korea Summit includes development. It calls for rebalancing the world economy in terms of reducing the income gap between countries, in particular the developing countries and developed countries. This is different from rebalancing in terms of current account surpluses and deficits.

Growing Interest in the G-20 in Developing Countries

The interest of developing countries in the G-20 process and its potential is growing judging from the press coverage and interest at think tanks. At the same time, there is a wait-and-see attitude as to what the G-20 will be able to deliver. Seven G-20 countries are members of the G-77, the group that speaks for developing countries at the United Nations. Many of these G-77 members question the legitimacy of the G-20 and want all actions channeled through the U.N. The G-20 will affect the dynamics of the G-77 at the U.N. Thus, delivering on development would enhance the legitimacy of the G-20.

Features of Recent Growth in Developing Countries

Rapid growth in many developing countries in the two to three years before the global financial crisis was based partly on a strong export performance as export volumes jumped and commodity prices rose sharply. Many countries could pursue growth-oriented policies while maintaining a viable current account because of rising exports and remittances. For precautionary reasons, many developing countries added substantial amounts to their international reserves despite stagnant aid, though the desire to maintain export competitiveness also probably played a role.

During the financial crisis, developing countries as a whole experienced decreased export earnings and outflows of private capital as well as declines in remittances. However, the larger developing countries, which are by and large members of the G-20, have shown considerable resilience and have returned to a robust growth path. This contrasts with the performance of the developed countries and many smaller developing countries, where there has been a recovery, but one which remains weak and fragile.

The issues before the G-20 Summit at Korea are to fulfill the promise of strong sustainable and balanced growth by spreading robust growth to the weak economies.

Short-Term Issues

The main short-term issues for the G-20 are pushing ahead with the reform of the global financial system and rebalancing of the economies. Reform

of the financial system has proceeded, catalyzing on the work already done by national and international institutions. The developing countries seem to have agreed to the processes and nature of these reforms, as they are based on analysis and experience and also as there seems to be sufficient leeway for individual countries to adopt measures consonant with their needs.

The need to tackle current account imbalances remains problematic and there is no full agreement yet on the means. Immediate fears about an outbreak of currency wars seem to have abated with the recent agreement among G-20 finance ministers to move toward more market-determined exchange rates. However, countries such as Brazil and India are calling for international action to deal with large capital inflows. There seems to be growing recognition by these and other countries that more policy coordination is needed at the international level to deal with issues such as current account imbalances and capital flows. But further development of the necessary international institutional arrangements for undertaking such coordination may be required before agreement on coordination measures can be reached.

Long-Term Issues

Rebalancing current account imbalances is a vital issue. Over the longer term, rebalancing will occur when there is a shift to development strategies that place greater reliance on domestic demand. Faster growth in poorer developing countries as called for by the agenda for Korea may need to be supplemented by using surpluses to balance deficits that may result from this faster growth.

Financing of Higher Levels of Investment

Growth could be fostered in lagging developing countries by higher rates of investment, financed by the restoration of aid flows and improving the access of these countries to private capital markets. Aid by itself would help maintain a credible balance of payments position and so encourage private flows. Another possible source for increased investments in the poorer countries could be the excess savings of surplus countries. Reduction of, say, the U.S. deficit would be achieved without increased consumption in China, which is possible only in the longer run, but by larger deficits in other developing countries, many of whom are currently running surpluses or very small deficits.

Aid Effectiveness

The G-20 should not only look at the quantity of aid but consider ways to increase its effectiveness. Aid for agriculture and infrastructure has been declining in importance.

The G7 has already called for increased aid to agriculture. The Seoul G-20 Summit is likely to call for increased investment in infrastructure. Increased aid for agriculture and infrastructure is likely to raise aid effectiveness, which could be further enhanced through governance reform both in the recipient countries as well as multilateral and bilateral donors. For instance, poverty in the middle-income countries may be more effectively tackled not by more aid but improving its delivery through civil society involvement. Remittances are effective in raising investment levels in the recipient countries and more remittances could be encouraged through reducing the cost of transfers. Strengthening aid for trade and a time frame for untying all aid are other issues that the G-20 could consider.

Foreign direct investment flows are more effective in raising growth than domestic investment. The G-20 should discuss what measures can be taken to increase FDI flows, particularly to smaller poor countries, which have very limited access to international financial markets.

Growth and Productivity in Agriculture

Growth in the poorer countries is very closely related to agricultural performance as borne out by the experience of countries in sub-Saharan Africa. Poor

performance of GDP in the 1980s and 1990s and better performance more recently were mirrored by agricultural growth. There has been a substantial slowdown worldwide in growth of agricultural output, causing sharply increased prices in 2007-08 and leading to calls for the need to improve food security. Investment in agriculture could be raised through more foreign aid for the sector. The shift in aid toward humanitarian assistance has been self-reinforcing in that when less aid goes for production, production shortfalls are more frequent or of a greater magnitude, leading to the need for humanitarian relief. In these circumstances, larger allocations for productive purposes can occur in the short run only if the overall amount of aid is increased substantially, since in the short run humanitarian needs must be met. Raising the growth of agricultural output requires raising the rate of productivity growth since there is very limited scope for area expansion. Raising productivity requires better technologies and this in turn requires more support for research. The G-20 needs urgently to put in place the necessary reforms as pinpointed by evaluations of the Consultative Group for International Agricultural Research.

One of the issues in raising productivity in developing countries is that of technology transfer, which is also important for higher productivity in industry and increasingly for reducing emissions and limiting the damage caused by climate change. The G-20 might need to look at rules governing intellectual property rights to examine whether the relative balance between innovators and imitators needs adjusting.

Conclusion

There is growing interest in developing countries in the potential of the G-20 in meeting the needs of international economic governance. But there is uncertainty as to what the G-20 will be able to achieve. Tackling development issues would help in increasing its legitimacy in the eyes of countries excluded from the G-20. There is broad agreement on the need to tackle the issues of economic imbalances, though countries differ on the relative importance of current account surpluses and deficits, the effectiveness of currency movements in dealing with this problem and the large capital inflows into many developing countries. Many of these issues are interrelated and point to the need for more policy coordination. Agreement on restructuring of the growth processes of development so that there is greater dependence on domestic demand might be more easily achieved if the growth rate is raised in many poorer countries, where growth is still weak and fragile. Increases in aid, greater access to private capital for these economies, and the development and spread of more productive agricultural technologies would all contribute to raising the growth rate.