

# Global Governance and the Reform of the International Financial Institutions

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Testimony to the European Parliament

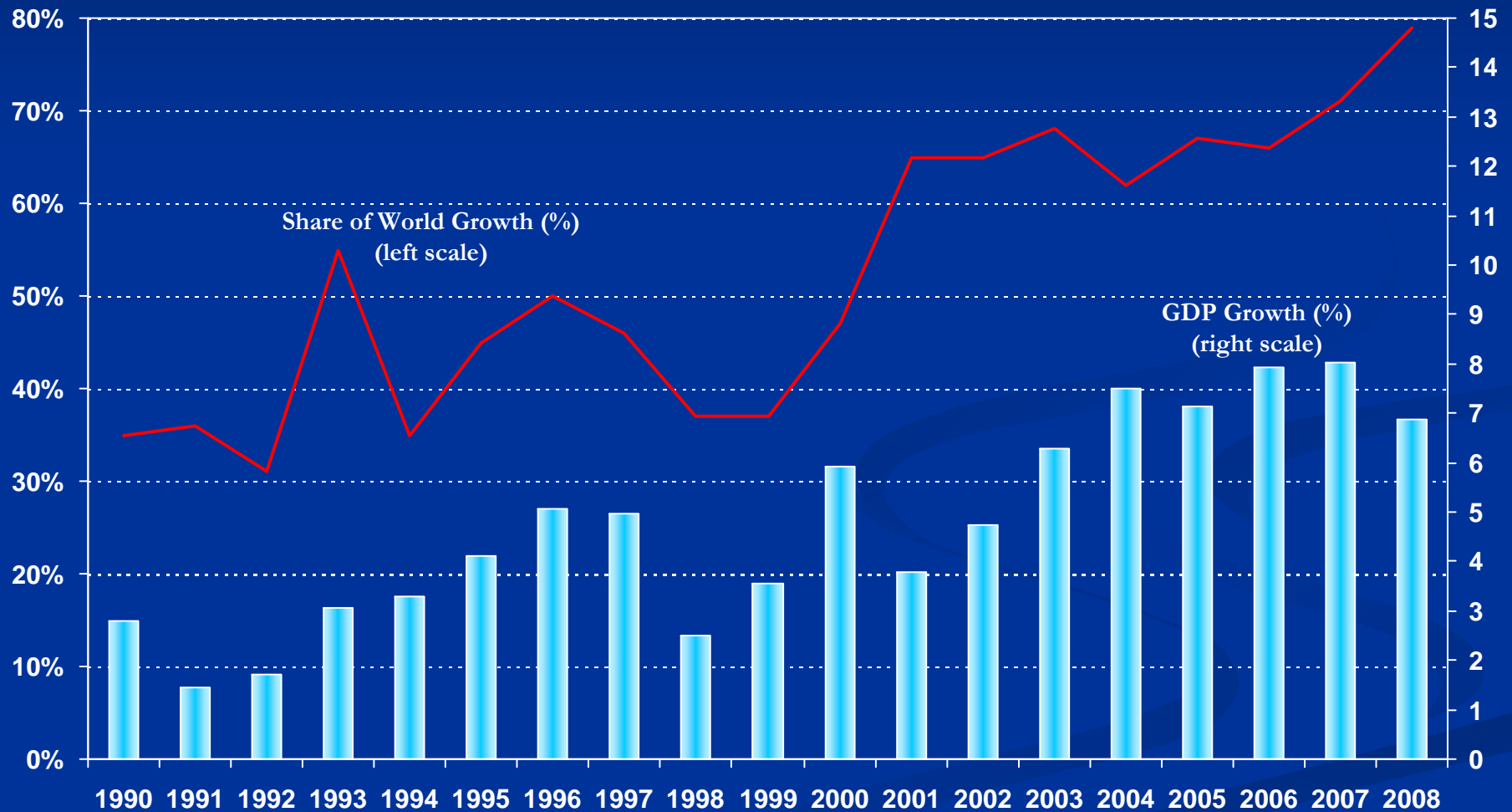
Special Committee on the Financial, Economic and Social Crisis

March 25, 2010

# Development Context

- Improved growth performance and debt sustainability across both middle and low-income countries
- Persistence of development gaps some warranting concessional financing
- Unmet global public goods linked often to domestic public goods

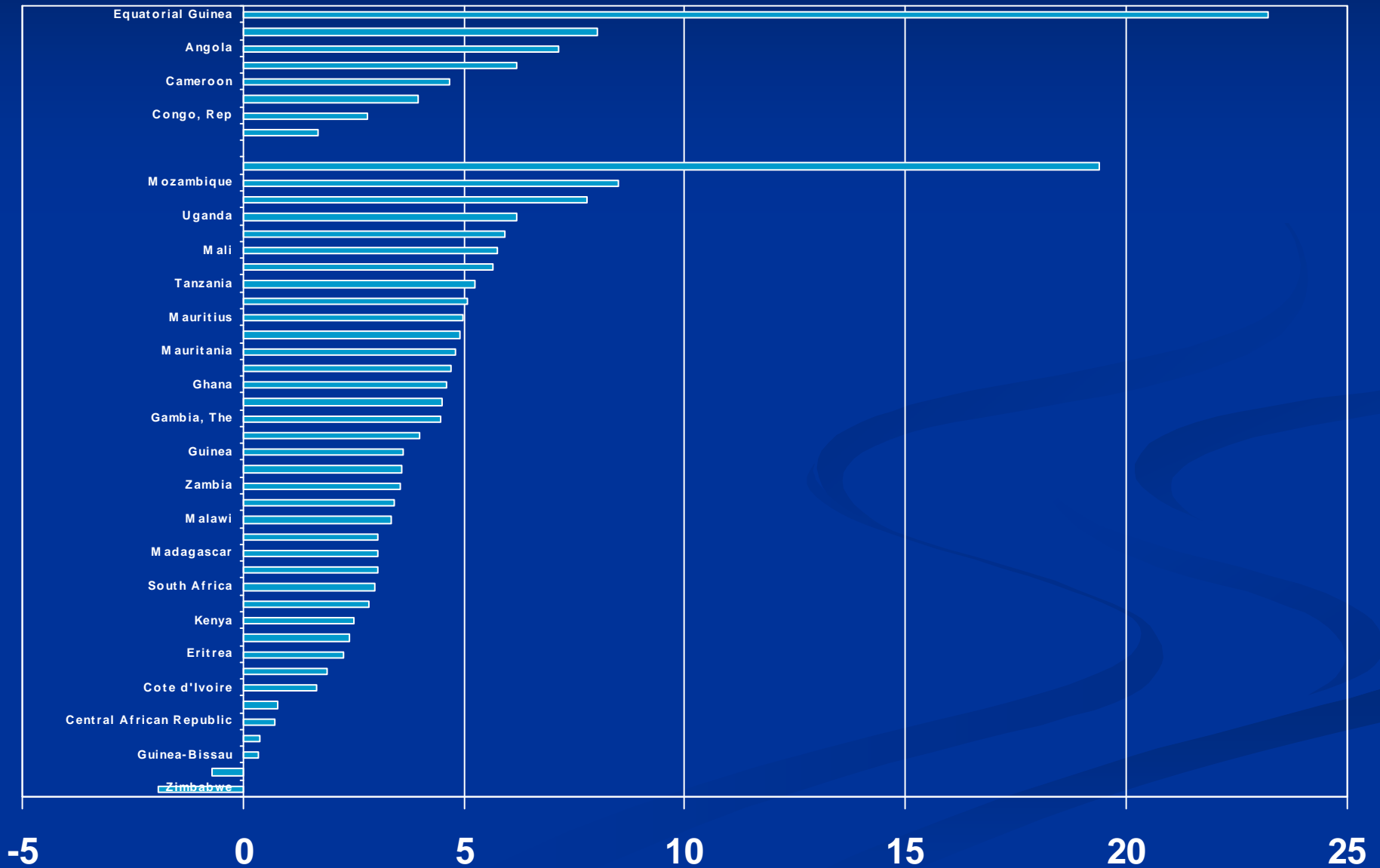
# Contribution of Developing Countries to Global Growth, 1990-2008



# Strong Growth Across the Developing World

	Average Growth	Number of Countries		
	2003-2008	>6	4-6	<4
MICs	5.7	28	39	19
LICs	5.1	20	15	13

# Average Annual GDP Growth in sub-Saharan, 1996-2005 (Percent)

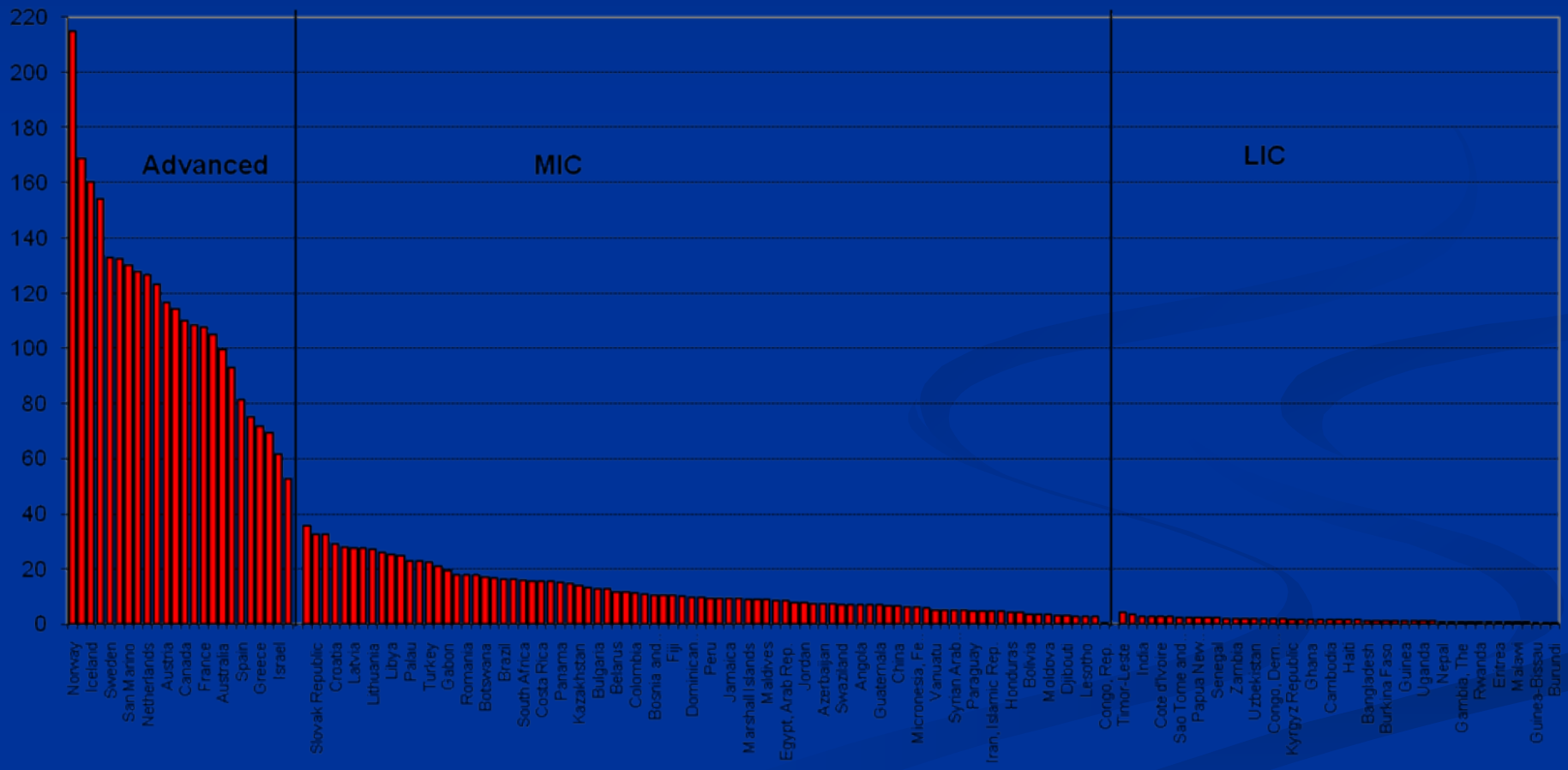


# Despite Progress Large Development Gaps Remain

	Population (Billions)	Avg. Per Capita Income per day (Current US\$, 2007)	Proportion of World's Poor (Percent, %)
Advanced	0.9	114.0	0.0
MICs	4.5	9.2	78.5
LICs	1.1	1.5	21.5

# Magnitude of the Income Gap

Per Capita Income / day  
GNI per capita, Atlas method (current US\$) 2007



Source: WDI, WB

# A Brief History of the G20

- Established in 1999 as a Finance Ministers and Central Bank Governors forum together with the Financial Stability Forum
- Preceded by G22 set up in the aftermath of the East Asian financial crisis
- From dialogue to consensus to global Steering Committee on economic and financial cooperation
- This evolution had started even before the crisis but major gaps as evident from the crisis in both macroeconomic coordination and financial sector regulation
- Crisis has given the group new impetus by raising it to the leaders level who have declared that it will be the “premier forum for international economic and financial cooperation”

# G20 Structure and Process



# G20: Significant Achievements but Many Challenges

## Achievements

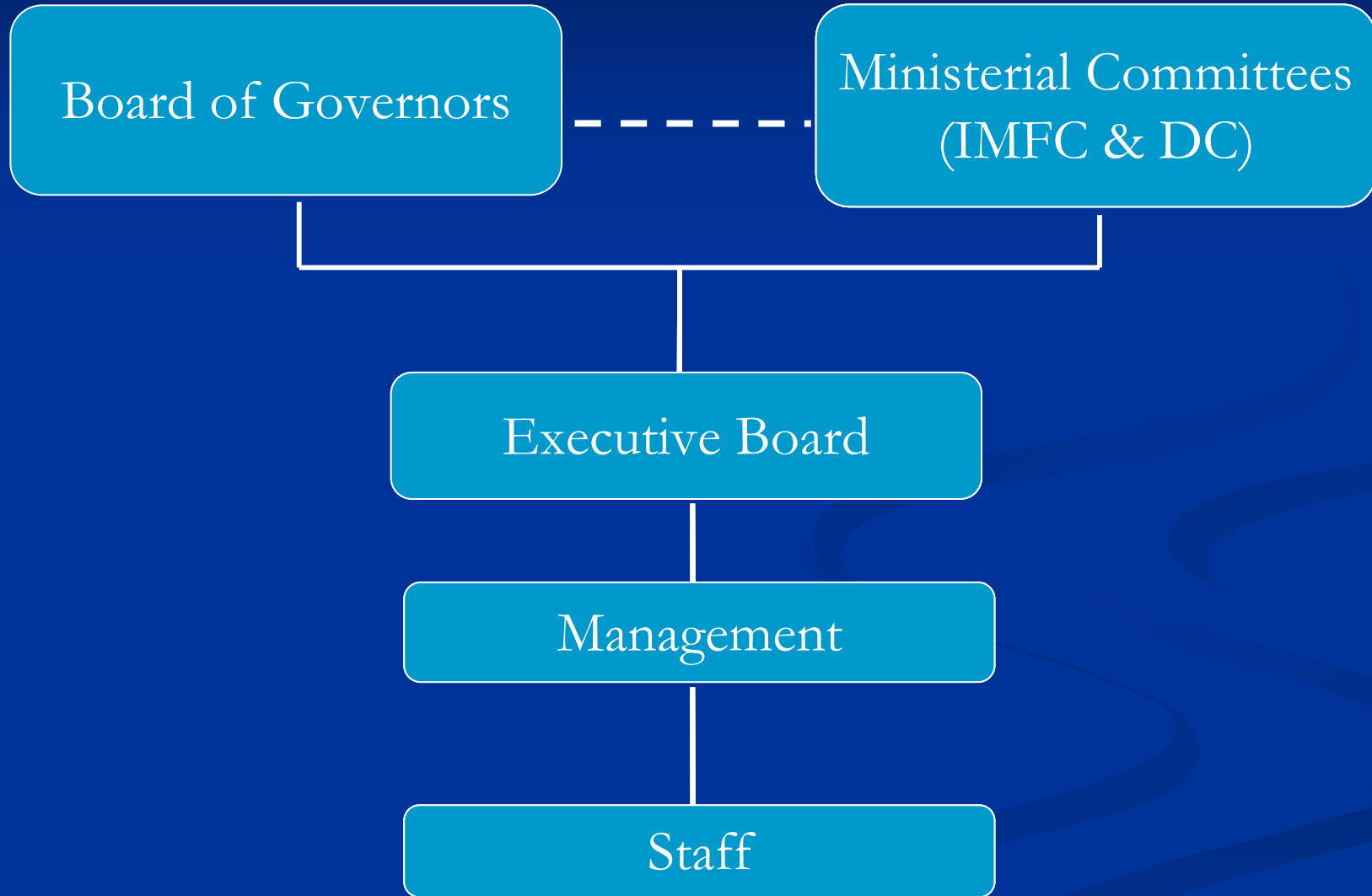
- Largest and most coordinated monetary and fiscal stimulus in history
- Commitment to, blueprint for and initial steps on fundamental reform of the financial sector
- Unprecedented resources for the IFIs (more than tripling of IMF resources, \$100 billion additional lending by the MDBs)

# G20: Significant Achievements but Many Challenges

## Challenges

- Coordination on exit strategies
- Implement framework for strong, sustainable and balanced growth
- Implement financial sector reforms in a globally coordinated way backed by peer review process
- Reform of international financial institutions
- Whether to extend role in other critical areas such as trade and climate change including climate finance
- LEGITIMACY AND INCLUSION

# Governance of IMF & World Bank



# Key Weaknesses in IFI Governance

- Insufficient Ministerial engagement and power imbalance vis-à-vis other fora
- Ambiguity of roles amongst the various constituent bodies
- Unbalanced representation (voting power, Board composition, decision rules, selection of Heads and Senior Management)
- Insufficient transparency
- Weak Board, management and staff accountability

# Manifestations of Weaknesses—IMF

- Lack of agreement on basic mandate
- Ineffective and asymmetric surveillance (including macroprudential monitoring and coordination)
- Lack of agreement on lending role (EMEs and LICs) including on conditionality and lending policies
- Limited progress on voice and governance
- Lack of intellectual openness

# Manifestations of Weaknesses—World Bank

- Rising “costs of doing business” and declining borrower demand
- IDA Deputies and “back door” conditionality
- Lack of legitimacy in tackling global public goods agenda, especially climate change
- Limited progress on voice and governance agenda

# The Global Plan for Recovery and Reform

## *G20 Leaders Summit, 2<sup>nd</sup> April 2009*

“...we are determined to reform and modernize the international financial institutions to ensure they can assist members and shareholders effectively in the new challenges they face. *We will reform their mandates, scope and governance to reflect changes in the world economy and the new challenges of globalization, and that emerging and developing economies, including the poorest, must have greater voice and representation.* This must be accompanied by action to increase the credibility and accountability of the institutions through better strategic oversight and decision making.”

# G20 Leaders/IMFC Mandate on IMF Governance Reform

“we support a shift in quota share to dynamic emerging market and developing countries of at least five percent from over-represented countries to under-represented countries using the current quota formula as the basis to work from. We are also committed to protecting the voting share of the poorest members. We urge all members to promptly consent to the still pending 2008 quota and voice reform.”

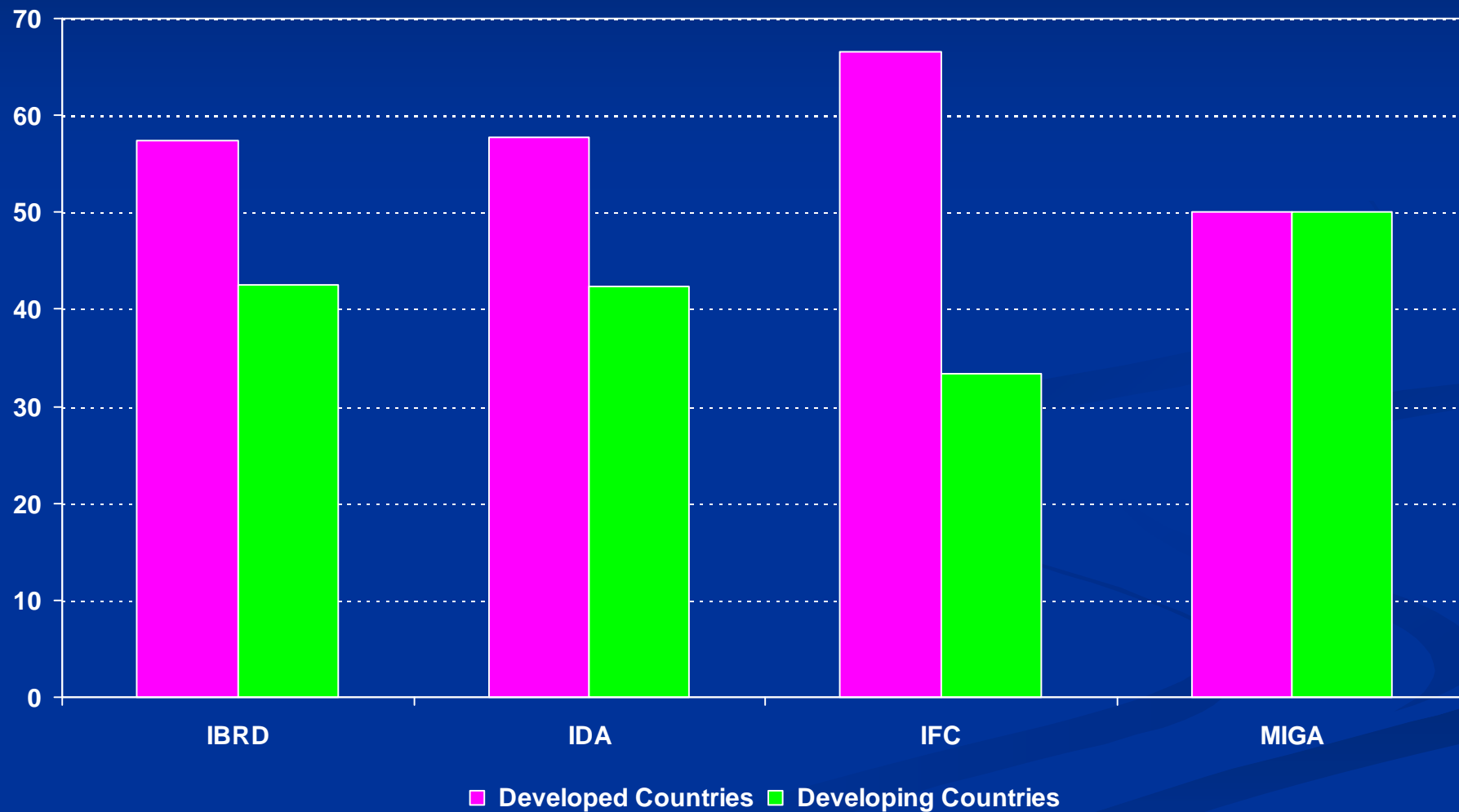
From IMFC Communiqué  
October 4, 2009

# G20 Leaders/Development Committee Mandate on World Bank Governance Reform

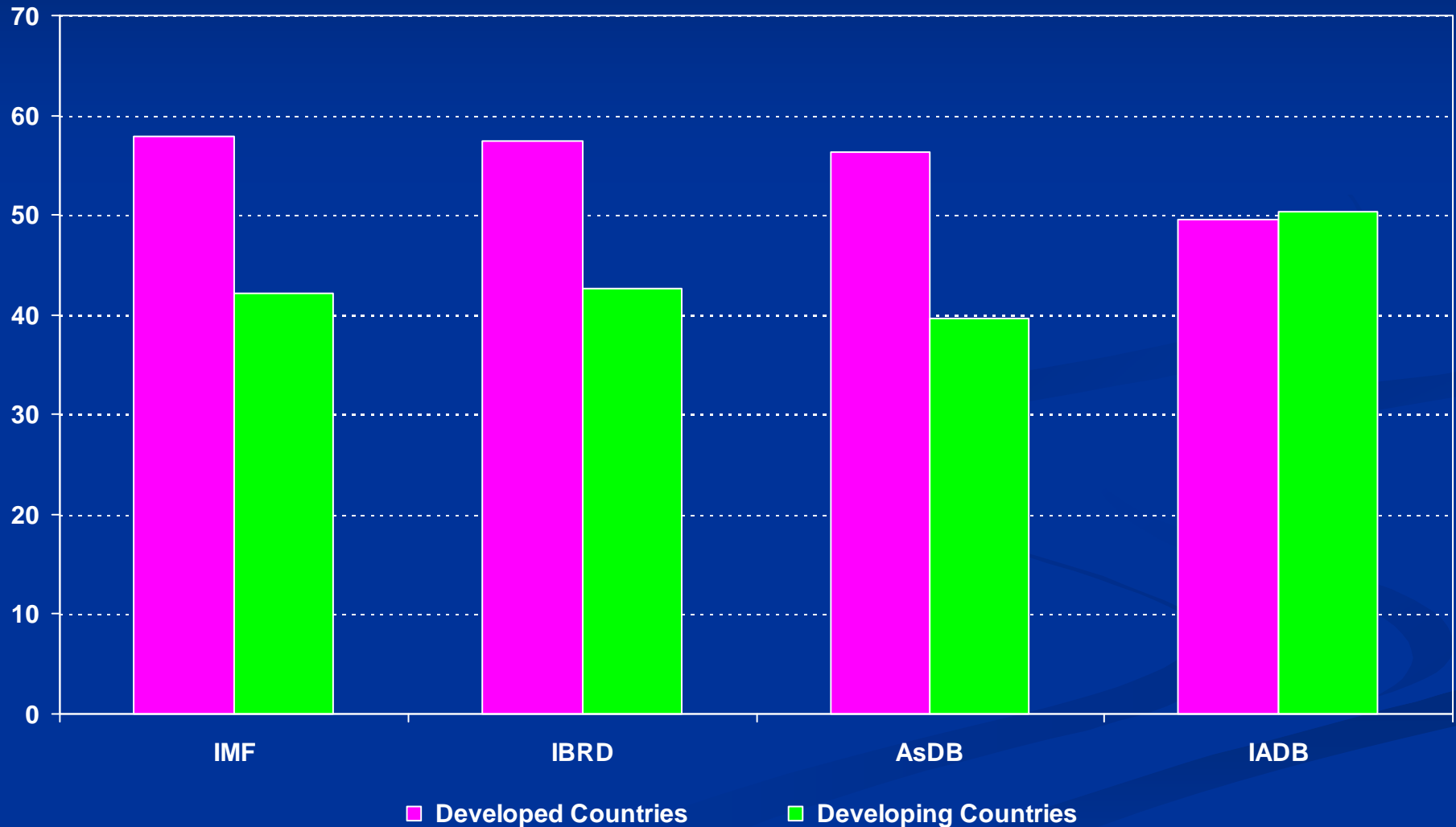
“stressed the importance of moving towards equitable voting power in the World Bank over time through the adoption of a dynamic formula which primarily reflects countries’ evolving economic weight and the World Bank’s development mission, and that generates in the next shareholding review a significant increase of at least 3% of voting power for developing and transition countries... [while protecting] the voting power of small poor countries”

From Development Committee Communiqué  
October 5, 2009

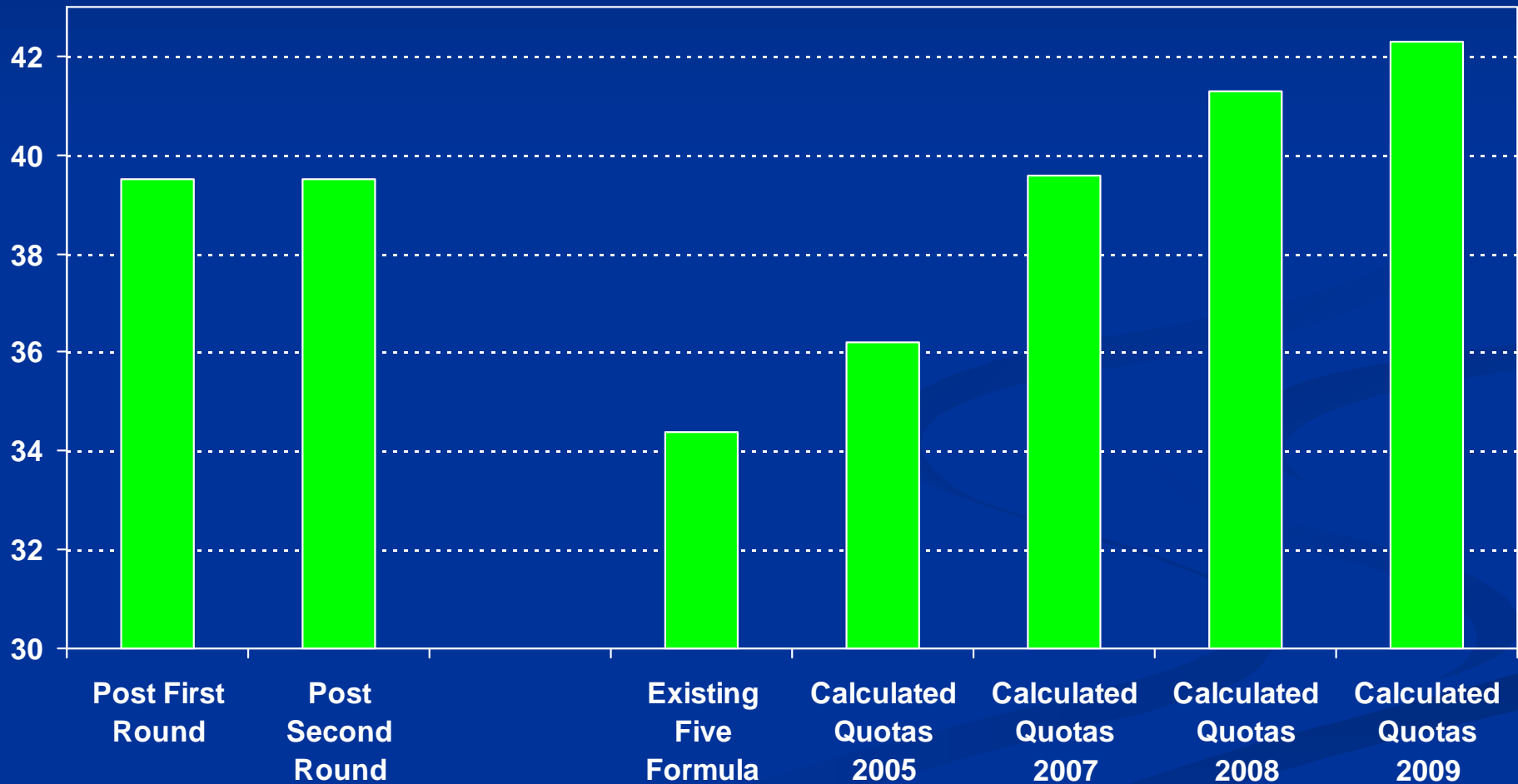
# Shares of Developed and Developing Countries in total Votes



# Total Votes for Developed and Developing Countries in Shares



# Impact of Recent Reforms and of Changes in Calculated Quotas on Quota Shares of Emerging Market and Developing Countries



# Who are Dynamic EMDCs?

GDP PPP 2006-08/ Post Second Round	GDP Growth 2003-2008		
	>6	4-6	<=4
<b>&gt;=1.2</b>	China India Vietnam Ethiopia Azerbaijan Bangladesh Kazakhstan Equatorial Guinea Russia Peru	Turkey Iran Colombia Brazil Egypt Indonesia Pakistan Poland Thailand Albania	Nepal Mexico Korea Spain United States
<b>1-1.2</b>	Lithuania Bhutan Angola Cambodia Estonia Belarus Turkmenistan	Dominican Republic Guatemala Greece Philippines Ecuador Botswana Burkina Faso Paraguay	Japan
<b>0.8-1</b>	Latvia Qatar Slovak Republic Sudan Tanzania Argentina Myanmar Romania Chad Uzbekistan Lao, People's Dem. Republic Ukraine United Arab Emirates Montenegro	Tunisia Chile Oman Macedonia, FYR South Africa Czech Republic Costa Rica Honduras Bolivia Morocco	Syrian Arab Republic El Salvador Australia Italy Portugal

# Dynamic EMDCs by Region

(in percent)

Asia	Quota Share <sup>a</sup>	LAC	Quota Share <sup>a</sup>	MENA	Quota Share <sup>a</sup>	SSA	Quota Share <sup>a</sup>	Transition	Quota Share <sup>a</sup>
China	4.00	Peru	0.27	Turkey	0.61	Ethiopia	0.06	Kazakhstan	0.18
India	2.44	Colombia	0.33	Iran	0.63	Equatorial Guinea	0.02	Azerbaijan	0.07
Vietnam	0.19	Brazil	1.78	Egypt	0.40	Angola	0.12	Russia	2.49
Bangladesh	0.22	Dominican Republic	0.09			Botswana	0.04	Lithuania	0.08
Cambodia	0.04	Guatemala	0.09			Burkina Faso	0.03	Estonia	0.04
Bhutan	0.01	Ecuador	0.15			Nepal	0.03	Belarus	0.16
Indonesia	0.87	Paraguay	0.04					Turkmenistan	0.04
Pakistan	0.43	Mexico	1.52					Poland	0.71
Thailand	0.60							Albania	0.03
Philippines	0.43								
Korea	1.41								
<b>Total</b>	<b>10.65</b>		<b>4.27</b>		<b>1.64</b>		<b>0.29</b>		<b>3.79</b>

<sup>a</sup> Share in Post-Second Round Quotas

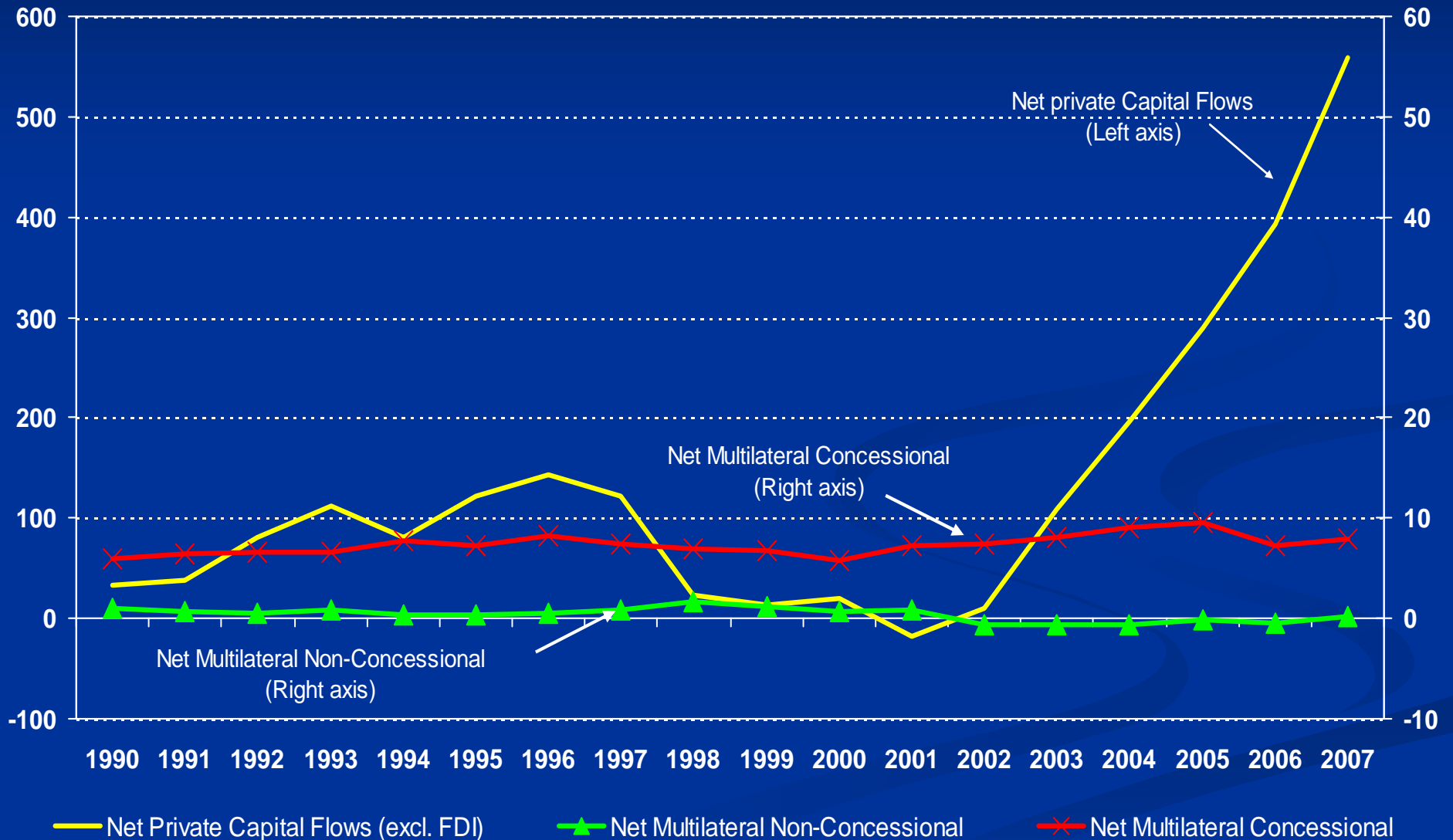
# Addressing Deficiencies in the Quota Formula

- There are three main deficiencies in the quota formula:
  - a) Economic dynamism is insufficiently recognized
  - b) Some advanced countries are improperly categorized as under-represented because of distortions in measures of openness and variability
  - c) Borrowers bear a disproportionate share of adjustment because variability is mis-specified
- These deficiencies can be addressed through adjustment within or outside the quota formula

# Reinvigorating the Development Mandate of the World Bank

- Promoting Knowledge Sharing and Institutional Development
- Coping with Volatility and Protecting the Vulnerable
- Scaling-up long-term development finance and countering the uphill flow of capital
- Meeting the challenge of global public goods

# Net Private Capital Flows (excl. FDI) and Net Multilateral Lending, 1990-2007 (Billions, US\$)



# Reform of Voice and Governance in the World Bank

- Initial package of reforms adopted at the last Annual Meetings (doubling of basic votes, partial offset for largest EMEs, and third chair for sub-Saharan Africa) was even more modest than the IMF with respect to voice and vote reform
- Discussions are now underway on a second phase of reform for implementation by the 2010 Spring Meetings
- Agreement must encompass and distinguish between IBRD, IDA and IFC

# Distinct Mission and Functions of the World Bank

	<b>IMF</b>	<b>World Bank</b>
<b>Mission</b>	International Financial Stability	Poverty reduction and development
<b>Functions</b>	Multilateral and bilateral surveillance Lending Technical Assistance	Global public goods related to development Market-based lending Concessional financing Policy advice and capacity building

# Criteria for a World Bank Specific Approach

- Equity in representation based on the development and poverty mandate of the World Bank
- Recognition of the development cooperative nature of the institution, i.e. taking into account the role of those that enable the Bank to carry out its mission as well as those that are important as clients in achieving the Bank's objectives

# Three Caveats on Current Discussions

- Economic weight is important but not the sole factor in determining representativeness or contribution/importance to the Bank's development mission
- Similarly IDA contributions are important but not the principal factor in enabling the Bank to carry out its mission
- Role of clients and especially the poorest countries need to be more explicitly recognized in voting power

# Towards a World Bank Specific Formula

## I. Representation Pillar

1. 1\$ = 1 Vote (GDP PPP and/or GDP MP)
2. 1 Country = 1 Vote (Basic Votes)
3. 1 Person = 1 Vote (Population or Square Root of Population)

## II. Development Cooperative Pillar

1. Contributions
  1. IDA
  2. ODA
  3. Outstanding IBRD Loans
2. Importance as Clients
  1. Incidence of Poverty
  2. Income status weighted by population

# Three Key Conclusions

- The IMF Quota Formula is Entirely Inappropriate for the World Bank
- A well specified Bank specific formula would entail a large shift in voting power today
- Selective reallocation with non-dilution should be the favored approach

# Additional Areas of BWI Reform

- Review of Mandate
- Size of resource base (quota for IMF, capital for World Bank)
- Size and composition of the Executive Board
- Strengthening of IMFC and DC
- Selection of Heads and Senior Management