Proposal for increasing developing country participation in global financial governance

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There are three areas where increasing developing country participation in global financial governance is urgent. The three areas are: 1) incorporating developing country participation in the Financial Stability Forum where at present they do not participate at all, even though they are invited to the working groups, 2) increasing participation of developing countries in the BIS (where there has been some, but clearly insufficient increase in participation) and in the Basle Committees (where there is no formal participation, though there has been increased consultation) and 3) enhanced participation of developing and transition countries in the IMF Board. This greater developing country participation would not only be clearly beneficial for developing countries themselves, whose voice would be stronger; it would also benefit the international institutions both by enhancing their legitimacy and also by getting valuable insights from developing countries; it would also benefit the developed countries, as they would ensure greater commitment from developing countries to free and open markets.

1. The Financial Stability Forum

In the wake of the Asian financial crisis, the Financial Stability Forum was created with three main purposes: 1) the identification of vulnerabilities in national and international financial systems and sources of systemic risk, 2) ensure that international rules and standards of best practice are developed, and gaps are identified and filled and 3) arrangements to ensure that consistency in rules across all types of financial institutions is improved.

The creation of the Financial Stability Forum is a very valuable step towards co-ordination of various bodies and actors to improve global stability. However, it is highly problematic that at present developing countries are not at all represented in the Forum itself.

Indeed, FSF membership is limited to three representatives from each G-7 country (one from the finance ministry, one from the central bank and one from the regulatory agency) one representative each from Holland, Australia, Hong Kong and Singapore (the latter two because they are a major financial centre). The IMF and the World Bank have two representatives each, as has the Basle Committee on Banking, IOSCO, and IAIS. The BIS, the OECD and the two other Basle Committees have one representative on the FSF. With the chairman, Mr Crockett, this implies a total size of 40 members at present.

At present the FSF does not include any representation from developing countries, even though many of these are major recipients of international private flows and all major crises in recent years have been in these countries. The FSF therefore is at present, a bit of a "Hamlet without the prince." There are therefore clear reasons why developing countries should be included. Furthermore, when the FSF was established by the G-7, they stated that "while the FSF initially would be limited to G-7 countries, it is envisaged that other national authorities, including from emerging market countries, will join the process at some stage."

There is a strong case to argue that the time has come for ensuring that this developing country participation takes place. Several G-7 countries are known to be sympathetic. Indeed, the Commonwealth Finance Ministers Meeting (in September 2000), which includes the UK, Canada, Australia and New Zealand, explicitly endorsed developing country participation. The Chairman of the FSF has also publicly expressed sympathy for developing countries' inclusion.

A specific formula could be proposed to include developing countries in the FSF. If six developing countries were included, the membership of the FSF would rise from 40 to 46, which is slightly more than 10 percent. Developing country representatives, for example from countries with large levels of private capital inflows in proportion to their GDP, could be chosen on a regional basis: there could be two Asian, two Western Hemisphere and two African. This would ensure that the perspectives of poorer countries would also be represented. These representatives could be appointed for a fairly short period (for example two years) and then rotated. This type of representation by developing countries operates in other contexts e.g. in the Boards of the Bretton Woods institutions.

The FSF is a very important initiative. Adding a small representation of developing countries to it would: a) increase its legitimacy, b) increase developing countries' commitments to its aims and c) add valuable insights and perspectives to its decision-making process. This would be achieved without a major increase of its membership.

2. The Bank for International Settlements (BIS) and the BIS Committees

The Bank for International Settlements is an increasingly important institution, as it has been increasingly active in the pursuit of its mandate to promote international co-operation on monetary and financial issues, with the pursuit of international financial stability at the heart of its activities. Initially the BIS activity focussed very much on financial stability in the major industrial countries, but has increasingly widened its activities to include developing countries; indeed the BIS has played an important role in both crises prevention and management, especially in the former.

Meeting in Basle, under the umbrella of the BIS - but not part of it - are three important Basle Committees. They are the Basle Committee on Banking Supervision (which produced the influential Basle Capital Accord), the Committee on the Global Financial System and the Committee on Payment and Settlements System.

The BIS was before 1996 constituted by the G-10 and Switzerland, as well as other developed countries, plus two developing countries, South Africa and Turkey. In 1996, several large developing countries were invited to join; they were Brazil, India, China, Korea, Saudi Arabia, Hong Kong, Mexico, Russia and Singapore. This is very welcome. However, there are at present no developing countries on the BIS Board of Directors (though there are no restrictions in the BIS statutes for this happening). There are very important monthly two-day meetings of G-10 governors; developing country governors are invited only to one session during the two days.

The Basle Committees define regulatory and other standards, that are increasingly implemented world-wide and that are increasingly becoming part of the IMF and World Bank surveillance of developing countries. However, the membership of these committees is still purely G-10, even though they do increasingly consult with developing and transition countries. Though they do consult, decisions are still being made by a purely G-10 group, decisions which then are implemented either via "soft law" and increasingly via IMF and World Bank surveillance (and possible future conditionality) by large numbers of developing countries.

It seems important and urgent to a) increase the number and types of developing countries who are members of the BIS. In the long term, this could even include universal membership, with weighted and rotating participation on the BIS Board. In the meantime, further increase of developing country participation in the BIS membership would be desirable, b) ensure participation of developing countries in the Board of the BIS and c) ensure greater and more formalised participation of developing countries in crucial meetings at the BIS, for example the monthly meetings of Central Bank Governors.

As regards the Basle Committees, which are currently made up of G-10 countries and Switzerland, these could be initially expanded to include one developing country representative for each region [Latin America, Asia and Africa]. These representatives could be appointed for a two year period and then the countries rotated. This would not excessively expand the size of the committees, and would allow crucial developing country participation.

It would seem important to achieve progress on several of these fronts, on the BIS and the Basle Committees simultaneously; this is not a particularly radical proposal, but just implies a fairly significant acceleration of recent trends.

Indeed, in some of these areas it may be easy to achieve agreement, as the BIS Senior Management and Board may well agree with some of these proposals. The problem may be of effective implementation. It may therefore be desirable to establish a small liaison group, for example between the BIS and a group representing developing countries, e.g. G-24 or G-77, who helps make concrete suggestions for creating mechanisms to ensure greater developing country participation in the BIS and the Basle Committees, along the lines suggested.

3. Enhanced participation of developing and transition countries in the IMF Board[1]

As is well known, the IMF is and will continue to be a key actor in the international financial architecture.

[1] This section has been jointly prepared with Ariel Buira, former Deputy Governor of the Banco de Mexico and IMF Executive Director. I also thank Bishaka MuKerjee for very useful suggestions.

Although the IMF is an international organisation, its members do not have equal voting power. The distribution of voting power in the IMF Board plays a key role in IMF governance.

The voting power of an IMF member has two components. Each member has 250 basic votes simply by virtue of its membership; this is a symbolic recognition of the principle of the legal equality of states. Each member also has one additional vote for every 100.000 SDRs of its quota. Because the number of basic votes has not been changed with successive quota increases, the ratio of basic votes to total votes fell from just over 11 per cent of the voting power of the 45 countries that participated at the 1944 Bretton Woods Conference, to less than 3 per cent in the 1990's, even though the total number of countries has at least tripled.

This is one of the important factors that has diminished the value of the initial principle of the legal equality of states, and has implied a rather low participation of developing countries in decision-making at the IMF.

The concentration of voting power in the hands of the major industrial countries ensure they have a determining influence on IMF policies. Furthermore, one country - the US - or in other cases a few major industrial countries, have actual veto power on a number of crucial decisions, such as the size of the IMF, policies on access to IMF resources, its scale and the rate of charge. As regards seats on the IMF Board, several small European countries are represented (e.g. Belgium, Netherlands and Switzerland each has a chair, even though they also represent other developing and transition countries). On the other hand, developing countries have a relative small presence (for example all of Sub-Saharan Africa has only two chairs, and Asia as well as Latin America only have three chairs). Small developing countries from the same region are also scattered (e.g. Central America) through different chairs, even though they often have similar problems and features.

A number of measures could be taken to improve both the distribution of quotas in general[2] and to enhance the role of developing countries in the governance of the IMF.

[2] An important recent document that addresses these first issues is the Report to the IMF Executive Board of the Quota Formula Review Group. April 18, 2000, also known as the Cooper Report, due to the name of its chairman

As regards the latter aim, to increase the role of developing countries and to make a more significant contribution to the principle of the legal equality of states, in the governance of the IMF it seems crucial to increase the ratio of basic votes to total votes in determining members' vote. Since this ratio was initially 11 per cent of voting power, when there were 45 countries, we suggest this ratio should be increased to 33% to reflect the fact that there are now over 150 countries that are IMF members. Should this figure be deemed too high by the major developed countries, compromise could be reached of an intermediate percentage - of 22% intermediate between the ratio of basic votes and the ratio of 33% that would reflect the large increase in IMF membership. This would be compatible with any formula for the quota distribution that will start being discussed, e.g. with the recommendations of the Cooper Report on Quota Review quoted above.