G20 Pittsburgh Summit
Emergence of the Emerging Economies

Sudipto Mundle

The recently concluded Pittsburgh Summit of G20 countries is notable for at least two reasons. First, a great deal has already been accomplished in implementing the global crisis management agenda that was adopted just five moths ago at the London Summit. It is an impressive achievement by any standard of global negotiations. Second, Pittsburgh marked the emergence of G20 as the premier forum for international economic cooperation, replacing the G7. A group of 12 emerging economies, including China, India, Indonesia, and South Korea from Asia, now have a seat at the head table along with the G7 and the European Union. What has been accomplished? How did we get here? What is the way forward from India's perspective?

The pace at which the London agenda is being implemented is quite remarkable, especially when compared to the protracted, gridlocked negotiations on climate change and the Doha Development Round on international trade. Moreover, the agenda is being implemented without a single formal treaty or even a formal institution. The agenda implemented so far covers three broad areas: a framework for strong, sustainable and balanced growth; strengthening the international financial regulatory system and modernizing the global development architecture. The growth framework is a framework for coordinating the fiscal, monetary, trade and structural policies of the G20 countries for achieving a balanced and sustainable global growth trajectory. The IMF has been tasked with assisting the Finance Ministers and Central Governors with its country performance surveillance and country policy analysis.

Strengthening the international financial regulatory system refers to a slew of country level measures to prevent the kind of regulatory failure and reckless risk taking that has led the world economy into a deep recessionary crisis. It includes higher and better quality capital requirements for banks; buffers against credit and asset price cycles; and tougher regulation of over-the- counter trade in derivatives, securitization, credit rating agencies and hedge funds, all of which contributed to escalating the current recessionary crisis. The proposed regulatory system also includes reform of compensation practices to prevent reckless risk taking by investment firms and development of internationally consistent, firm specific contingency and resolution plans for financial institutions that are large enough to generate systemic risk if they fail.

Modernization of the global development architecture refers to reform and strengthening of the IMF, the World Bank and regional development banks to enable them to better help the developing countries in coping with financial crises. A massive infusion of additional resources totaling nearly $900 billion is being provided, mostly throughb the IMF. Simultaneously, major reforms are underway as part of the IMF's ongoing quota review, to be concluded by January 2011. This includes, among other reforms, a shift of an additional 5% of its voting quota to dynamic emerging market and developing countries. Governance reform in the World Bank will include shifting an additional 3% of voting shares to developing and transitional countries. Also, the heads and senior staff of these institutions will henceforth be appointed through an open, transparent and merit based process. These reforms are important in strengthening the voice of emerging market and developing countries in the global development architecture.

These reforms in the multilateral financial institutions reflect the growing importance of emerging economies in the global arena, which also accounts for the replacement of the G7 by G20. How did this come to pass? In my last column (Mail Today 18 September, 2009) I had mentioned that one of the consequences of the current global economic crisis is an acceleration in the relative decline of the G7 vis-à-vis the emerging economy members of G20, especially China and India. The crisis has brought to a tipping point a process that has been underway for half a century. The pendulum of economic power that was swinging from east to west since the 18th century gradually reversed its direction after the Second World War. The rise of post-war Japan from the 1960s was followed by the emergence of the 'miracle economies' of East and South-east Asia, then the rise of China, and finally India at the close of the 20th century.

The rise of these Asian countries, and indeed all the emerging market economies within the G20, is entirely attributable to their high growth, relative to the rest of the world. There is a vast literature that debates the sources and causes of high growth. However there is little doubt that it is indeed high growth, sustained over a long period, that has finally won a seat at the high table of global economic management for the emerging economies. Reforms in the formal structures of geo-political power invariably follow the re-alignments in economic power with a time lag, in this case sixty years, since the declining economic powers resist change in the formal structures of power.

Eventually, the formal structures are reformed to align them with the realities of economic power, but the adjustment is seldom complete. Thus, even after voting reforms are implemented in the IMF, the US will still retain *de facto* veto powers with its 17% share since most decisions require 85% majority. US, EU and Japan will still retain a 53% majority of voting rights. Individually, the shares of US, Japan, U.K. and France will still exceed that of China. In other words, if the G7 are today prepared to share the high table with the emerging economies, they are not doing so out of any generosity but because of compelling circumstances. The emerging economies are today so large that it is no longer possible for the G7 to call the shots and manage the global economy without their cooperation.

These rules of the game are not going to change. Their higher growth and rising economic strength will enable the emerging economies to have a larger voice. However, such voice will not come to them as a gift on a platter. Instead they will have to wrest that voice for themselves, as they have done in Pittsburgh. There are important lessons in this as India positions itself to occupy its proper place in the global economy in the years ahead. It is quite likely that in the next two to three decades India will emerge as the third or fourth largest economy in the world. That relative economic position will anchor its position in the formal structures of global power. Sound diplomacy could help India win a voice that is commensurate with its economic power while weak diplomacy could leave it somewhat below its real weight. However it is India’s relative economic size, and hence its pace of growth, that will primarily determine its place in the world.

[The author is Emeritus Professor at the National Institute of Public Finance and Policy. *sudipto.mundle@gmail.com*]