G-24

The Developing Countries in the International Financial System

edited by
Eduardo Mayobre,
Central Bank of Venezuela

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LYNNE RIENNER PUBLISHERS
BOULDER
LONDON

Published in the United States of America in 1999 by
Lynne Rienner Publishers, Inc.
1800 30th Street, Boulder, Colorado 80301
www.rienner.com

and in the United Kingdom by
Lynne Rienner Publishers, Inc.
3 Henrietta Street, Covent Garden, London WC2E 8LU

Library of Congress Cataloging-in-Publication Data
G-24 : the developing countries in the international financial system
/ edited by Eduardo Mayobre.
Includes bibliographical references and index.
ISBN 1-55587-846-6 (hc : alk. paper)
1. International finance. 2. Finance—Developing countries.
3. Group of Twenty-four. I. Mayobre, Eduardo, 1946– .
HG3881.G128 1999
332'.042'091724—dc21 99-26297
CIP

British Cataloguing in Publication Data
A Cataloguing in Publication record for this book
is available from the British Library.

Printed and bound in the United States of America

The paper used in this publication meets the requirements
of the American National Standard for Permanence of
Paper for Printed Library Materials Z39.48-1984.

5 4 3 2 1

Foreword

The inaugural ministerial meeting of the Group of 24 (the G-24) was convened in Caracas in April 1972 at the invitation of the government of Venezuela. Twenty-five years later Venezuela again assumed the chairmanship of the group, and in February 1998 convened an extraordinary ministerial meeting.

There had been many changes, often important, in the international financial scene during that quarter-century, both reflecting and affecting the political and economic evolution of the world. Developing countries and their role in the world economy also had changed, but the concentration of decisionmaking power in a number of developed countries and the need for concerted action among the former remained the same. In its first ministerial declaration, the G-24 "expressed its dissatisfaction that important decisions affecting the International Monetary System have been taken by a small number of developed countries to the exclusion and neglect of the interests of the rest of the international community, and that these decisions have adversely affected the economies of developing countries." After the first 25 years, the Caracas Declaration II called for "the increased representation and participation of developing countries in the decision making organs of the international community to properly reflect developing countries' growing influence in the world economy."

The limited role of developing countries in international financial forums does not mean that those countries are unaware that it is their own actions that are key to solving their problems. The Caracas Declaration II emphasizes that "the prime responsibility for development and poverty reduction in the developing world continues to rest with the peoples, institutions and governments of the developing countries themselves." Nevertheless, part of that responsibility lies in ensuring that the needs and interests of those countries' peoples are properly considered in the shaping of international affairs. This book is an account of the efforts made by developing countries in the field of international monetary issues, a reflection on 25 years of hope, frustrations, and some modest achievements. It is also an examination of the present and future challenges of developing countries in a changing world.

With the increasing globalization of the world economy some developing countries have become more active in international affairs, while others face the risk of marginalization. What remains unchanged is that poverty and insufficient means for development are concentrated in a part of the world where the majority of the population lives, while the means of production and the decisionmaking power are concentrated in but a few countries.

This state of affairs is one of the reasons that developing countries feel the need for a coordinated approach to dealing with world politics, and the G-24 is one of the best examples of such coordination implemented in a sustained, serious, and technically sound way. The G-24 was constituted by the Group of 77, a forum of developing countries that coordinate their actions within the framework of the United Nations. The G-24's membership, reflecting a wide geographical range, represents the totality of developing countries. Its creation was a reaction to the breakdown of the Bretton Woods monetary system in the early 1970s and the subsequent turmoil in international financial affairs. The establishment of the G-24 was meant to achieve a greater and more active participation in the reform of the international system, which at the time was still being shaped by only a few members of the international community.

From the outset the G-24 recognized, as stated in its first ministerial declaration, "that the institution for decision making on international monetary matters should be the International Monetary Fund." Also from the beginning, the hopes raised by the prospect of an internationally concerted action for promoting world development and reducing poverty and income disparities led the G-24 to deal with matters not strictly monetary. For example, there was the creation of the Development Committee (or Joint Committee of the International Monetary Fund and the World Bank for the Transfer of Real Resources to Developing Countries), which was a landmark in this regard, as was recognizing the importance of the sustainability of growth.

This book reflects both the experiences of the developing countries with monetary matters and the ample agenda the countries face today. It reviews past actions and positions, but deals as well with issues of current interest and with matters that are seen as important for the future of international economic relations.

Chapter 1 traces the relationship of the developing countries with the never completed reform of the international financial system and with the multilateral organizations. Chapter 2 considers the future of the G-24: What should be its role as a forum of developing countries? What are the more important issues that it should address?

Chapters 3 and 4 look back at the role of income from oil exports and its circulation in the international financial system, a major determinant in the evolution of monetary and economic issues in the 1970s and 1980s. Chapters 5, 6, and 7 explore the early stages of the current Asian crisis through the lens of the national experiences of Indonesia and Korea, as well as in terms of its impact on Latin America.

Chapters 8 and 9 deal with the process of globalization as the general framework of international economic relationships. Chapter 10 then focuses on the new capital flows and emerging markets, and Chapter 11 discusses the volatility of private capital flows. Chapter 12 assesses the challenges faced by labor as a result of globalization and economic integration. In conclusion, Chapter 13 considers the sustainability of the development process.

The authors, all distinguished scholars from developing countries, have had direct practical experience in international relations and policy-making. Their familiarity with the endeavors of developing countries, and in particular with the actions of the G-24, provides insight into the continuing efforts of those countries to express, coordinate, and advance their positions and interests.

The Central Bank of Venezuela is very proud to have sponsored this volume, which it feels will contribute to a better understanding of the role of developing countries in international affairs. Special emphasis has been given to the means and possibilities for action and to the challenges and opportunities presented by the current international environment, particularly in relation to the international financial system. The occasion of the 25th anniversary of the creation of the G-24 provides an opportunity to present the points of view of developing countries on issues that are shaping our present and our future.

Antonio Casas-González
Chairman (1997–1998), Group of 24
President, Central Bank of Venezuela

Acknowledgments

William Larralde, chairman of the Deputies of the Group of 24, gave inspiration and guidance for the development of this book. G. K. Helleiner, professor of economics at the University of Toronto and head of the G-24 research program, gave invaluable advice. Aziz Ali Mohammed and Clara Pasquali, of the G-24 Liaison Office in Washington, D.C., and Alicia Garcia of the Central Bank of Venezuela provided technical and logistic support. I am deeply indebted to all of them.

Eduardo Mayobre

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PART 1

A Quarter-Century of Experience

1

The Developing Countries and the International Financial System: 25 Years of Hope, Frustration, and Some Modest Achievements

Francisco Suárez Dávila

In 1997, the intergovernmental Group of 24 (the G-24)* reached an institutional life of 25 years, having met first in April 1972 in Caracas. After a quarter-century, Venezuela again held the chairmanship.

During this quarter-century, some of the most dramatic changes in history have occurred; but in some respects there have been no changes at all. In 1972 the developing countries played a very small role in international monetary affairs. Their share in world trade was around 25 percent; in international reserves, 22 percent; and in International Monetary Fund (IMF) reserve positions, 16 percent. They were represented by only nine out of twenty executive directors on the boards of the Bretton Woods institutions. The developing countries had for the most part fixed-exchange or multiple-currency practices and exchange controls, and their levels of international debt were reasonable. The Bretton Woods system had been dealt a serious blow in 1971, with the suspension of dollar convertibility. In the succeeding years, the developing countries became key players in the energy crisis of 1973 and the debt crisis of 1982. Two new Bretton Woods institutional bodies were created: the Interim Committee and the Development Committee. Par values of currencies were replaced by widespread floating, but with a consolidating process leading toward the dawn of European monetary union. Some years later the Berlin Wall fell, and now even the former socialist economies are players in the system and have joined the IMF and the World Bank. There are now industrial, transitional, emergent, and developing countries. The international financial system has been affected by the "first crisis of globalisation into the 21st century"—the

*The Group of 24 is made up of: Algeria, Argentina, Brazil, Colombia, Congo (formerly Zaire), Côte d'Ivoire, Egypt, Ethiopia, Gabon, Ghana, Guatemala, India, Iran, Lebanon, Mexico, Nigeria, Pakistan, Peru, Philippines, Sri Lanka, Syrian Arab Republic, Trinidad and Tobago, Venezuela, and Yugoslavia (currently inactive).

Mexican events of 1994—and already another crisis has erupted, also related to massive capital outflows and affecting what had hitherto been considered the "wonder" side of the world economy, the Asian "tigers." To top it all, the traditionally booming Japanese economy has been suffering from a period of stagnation.

Even though the developing countries have grown in economic importance—and there is now recognition of a new group, the Group of 5 (China, Russia, Brazil, Indonesia, and India), with its increasing share of world trade and gross domestic product (GDP)—some of the old problems remain unchanged. There is the problem of balance, which is perhaps now related more to capital, the need for the transfer of real resources being more pressing due to the growing inequality between the industrial and more advanced developing countries. The debate continues about the IMF's oversight and its lending conditions, as well as the role of the Bretton Woods institutions. The Group of 7 (G-7)* (and not even the G-10†) goes on making major system resolutions by itself. There is still the argument about lack of participation by LDCs (less developed countries) in the decisionmaking processes in regard to the main economic issues. There has been the shift from the Keynesian *pensée unique* toward "neoliberal" thinking and its prominence in Washington, D.C. (though there are now signs of some rethinking). Most recently, economic globalization, with its benefits and costs, the increasing concern about social cohesion, and the requirements of the environment and sustainable development are demanding close attention. Just these few issues illustrate the evolution of the world scene that occurred between the first and the 58th meetings of the G-24. With this background we will survey the group's history.

The Role of the Developing Countries in the *Belle Époque* of the International Financial System (1946–1970)

It is generally assumed that the developing countries did not play a role in the early stages of postwar international monetary cooperation. However, their participation at the Bretton Woods Conference was important. Forty-four countries participated, including all the Latin American countries and India, Iraq, Iran, China, Egypt, Ethiopia, and the Philippines. All played a role in the conference committees. John Maynard Keynes chaired the one for the World Bank and Harry White the one for the IMF, but a third committee, dealing with other means of international financial cooperation, was chaired by Mexican Finance Minister Eduardo Suárez. Among other

*G-7: United States, Great Britain, Germany, France, Italy, Japan, and Canada.
†G-10: The G-7 plus Sweden, Belgium, and the Netherlands.

topics, this committee had to deal with the problem of silver, of importance to developing countries like China and India. The major contribution was the Mexican proposal presented in the session of 12 July that the Bank for International Reconstruction, geared to European reconstruction, should also be used for *development.*[1]

In the consideranda for the proposal two important points were made:

1. "In the short term, possibly reconstruction will be more urgent for the world in general. But in the long run, before we are all dead [a reference to the Keynesian phrase], the concern for development will prevail."
2. "We have supplies of gold and international reserves in unprecedented levels; we speak for the Latin American countries. We can devote these resouces to import capital goods for our development but we want our projects to be put on an equal footing with reconstruction."

Hence, the World Bank became the International Bank for Reconstruction and *Development* (IBRD).

Over the succeeding years, the developing countries benefited from the *belle époque* period of world growth of the 1950s and 1960s, pushed forward by Marshall Plan aid and European reconstruction, the Korean War and Asian reconstruction and development, the process of European integration, and resource transfers related to the Cold War competition and the initial period of dollar "glut." The developing countries adapted their economies, with different institutional arrangements (e.g., central planning, mixed economies) and varying degrees of economic success, during what for many countries in Asia and Africa was the first "transition" from colonialism to independence (the second transition being from socialism to a market economy).

The system started to show signs of strain in the late 1960s, with the dollar shortage and problems related to the insufficient stock of gold and the fiscal and external deficits of the United States aggravated by the war in Vietnam.

Since the mid-1960s the G-10 deputies, under the leadership of Otmar Emminger and Rinaldo Ossola, had been working on the creation of international reserve assets to replace the dollar in the international reserves of major countries. The resulting idea was to create the special drawing right (SDR), but the initial proposal was to have a limited distribution, mainly to G-10 major industrial countries.

The developing countries had been engaged in preparation for a special United Nations Conference on Trade and Development (UNCTAD I) to be held in Geneva in 1964. For this meeting, the Group of 77 (soon to be increased in number) was created as the forum to coordinate the positions of the group's members. One of the first actions was to push for creating an SDR that should have universal distribution and to discuss SDR rules within the IMF. The smaller European countries supported this view.

The principle was finally agreed on, and joint meetings took place between the G-10 deputies and the Executive Board of the IMF. This led to another important mechanism to coordinate the views of the developing countries: the G-9, the group of executive directors representing developing countries on the board of the IMF and the World Bank. The Articles of Agreement were amended in July 1969, and the first distribution of SDRs to all the IMF members began in January 1970. Thus, the first stage of cooperation in international monetary affairs by LDCs—to prevent decisions affecting the entire system being made by only a few countries—had been achieved. It was the first important institutional result.[2]

The proposal also was made that there should be a *link* between the creation of SDRs to satisfy the liquidity needs of the system and the transfer of real resources to developing countries.

The Creation of the G-24: How the LDCs Organized to Participate in the International Reform Process (1971–1972)

The unilateral decision by the United States government in August 1971 to officially suspend the convertibility of the dollar to gold gave a severe shock to the system, and essentially dealt a death blow to it as it had been functioning since Bretton Woods. In the Smithsonian Agreement achieved in Washington, D.C., by the G-10 ministers a new currency alignment was achieved between the falling U.S. dollar and the appreciating Japanese yen and European currencies. There were also two important decisions: (1) to initiate discussions about the reform of the international monetary system, and (2) to carry out reform with meetings between the G-10 and the Executive Board within the framework of the IMF. In September 1972 the IMF Executive Board presented a document setting out the issues for the reform of the system, and the Committee of 20 to negotiate that reform was created on 18 September 1972.

After the Smithsonian "shock" the tempo of meetings and negotiations among developing countries also increased. The first step toward the creation of the G-24 was the second ministerial meeting of the G-77 held in Lima, in November 1971, where the decision was taken to create a special group to consider international monetary issues. That body approved the declaration and principles of the Action Program of Lima, which contained a statement on a theme that unfortunately would recur from time to time: "It is entirely unacceptable that vital decisions about the future of the international monetary system, which are the concern of the entire world community, are sought to be taken by a limited group of countries outside the framework of the IMF."

Discussions then took place to establish the characteristics of the new negotiating group of developing countries. The preparatory meeting of deputies of the Intergovernmental Group of 77 on International Monetary Affairs took place in Geneva, chaired by the representative from Peru, and set out a tentative program and a working structure that had as basic elements the following:

1. There would be two levels of discussion: the deputies at technical level and the ministers to achieve political consideration.
2. Both levels would have a chairman and a deputy chairman. The ministers would have a second deputy chairman and the deputies a rapporteur.
3. Regional representation would be achieved by having eight members per region.

The first meeting of the G-24 was held in Caracas, at deputy level, 3–5 April, and at ministerial level, 5–8 April 1972. The ministerial meeting was chaired initially by the foreign minister of Peru, Guillermo Marco del Pont. After the election, Pedro Tinoco, minister of finance of Venezuela, became chairman; M. S. Mostefai, governor of the Central Bank of Algeria, and W. N. Perera, minister of finance of Sri Lanka, became vice-chairmen. Carlos Rafael Silva of the Central Bank of Venezuela, who had been previously elected chairman of the deputies, acted as rapporteur. Lal Jayawardena, who in the future was to make frequent contributions to the intellectual work and the participation of the LDCs in the reform process, was elected vice-chairman of the deputies. M. Falegan of Nigeria acted as rapporteur. It was an important shift in the framework of the G-77 to have established a specialized body of finance and central bank officials to carry on the work related to international monetary affairs. Pierre-Paul Schweitzer, managing director of the IMF, and Manuel Perez Guerrero, the secretary general of UNCTAD, attended the meeting. The work of the G-24 would be supported in the future by the staffs of the two institutions.

The group referred to several procedural and substantive aspects in its first communiqué:

1. The group considered that the most important task facing it at the moment was to provide for fundamental improvements in the decisionmaking process regarding international momentary issues. The group agreed that the institution for decisionmaking on international monetary matters "should be the International Monetary Fund" and unanimously favored the creation of a committee of a board of governors of the IMF (the Committee of 20)

2. It supported the idea of a new activation of SDRs from 1 January 1973 determined by the liquidity needs of the world economy.
3. The group gave its fullest endorsement to the establishment of a link between SDRs and additional development finance.
4. It expressed its dissatisfaction with the present system of developing country IMF quotas.

At the UNCTAD III held in Santiago de Chile three weeks later, the communiqué was endorsed.

The G-24 had its second meeting in Washington, D.C, preceding the first meeting of the Committee of 20 on the reform of the international monetary system, a feature that would become a *modus operandi* of the group. By the time of that meeting, reports had been prepared by the deputies, relating to the main points stated in the first communiqué: the objectives of the reform of the system, allocation of SDRs for a second basic period, net transfers of financial resources, and the quota structure of the IMF.

A number of technical papers had been prepared by a very well-qualified group of experts that would continue to play a role in the future: Sidney Dell (UNCTAD), Carlos Massad (Chile), Ricardo Arriazu (Argentina), and Alfredo Phillips (Mexico). Professor Robert A. Mundell and E. M. Bernstein had papers commissioned by the Bank of Mexico; however, the topics at that early stage were still quite limited.

From the "Unreformed" International Monetary System to Its Evolutionary Process (September 1972 to 1982)

After September 1972 there was a period of hope, when it was considered possible to construct the blueprint for a new international monetary system to replace Bretton Woods. Those hopes were shattered after the dramatic adjustments and the instability that followed the sharp increase in oil prices at the end of 1973. After January 1974, there was a search for an interim solution, which took basic shape in the Accord of Jamaica in January 1976. Afterwards immediate "reform" gave way to an evolutionary process for the system. If one compares the basic objectives for negotiation and the features that finally emerged in the system, one can appreciate how much the results deviated from the initial path and how far the vehicle of reform wandered from its destination:

- For the "exchange rate" policy, there was an attempt to substitute the par value system for one of fixed but adjustable rates. This in turn gave way to a system of floating guidelines. The system