G20

MAYO 2024

Finance track

STUDY GUIDE

Letter from the Executive Board

Greetings Delegates,

Welcome to the Finance Track at the second Mayo Model G20 summit. Our goal is to illuminate the path to a brighter future for our planet and its inhabitants. I am Raj Anand Kataruka, moderating this track along with Paarth Gupta and Divit Chandak.

The Global Financial Architecture comprises institutions, regulations, and mechanisms that govern international financial transactions. It includes organizations like the IMF, World Bank, and regulatory bodies shaping the global financial system.

Our mission is to aid global development. We expect delegates to propose innovative yet practical ideas, balancing creativity with deep knowledge of current financial systems. Successful delegates will combine unique ideas with diplomacy, constructive paperwork, and effective lobbying.

The topic is open-ended, encouraging ideas that consider global and economic factors. Detailed research will fuel heated debates and negotiations. This background guide is just the starting point for your research.

We aim to moderate the track in an exciting yet practical manner. Use the committee's broad-mindedness to craft an architecture fostering global development, truly embodying “Building a Just World and a Sustainable Planet.” We eagerly anticipate your contributions.

Regards,
Moderators, Finance Track

About the Committee

In today's age of unprecedented technological advancement, unparalleled interconnection and complex geopolitical dynamics, the need to revolutionise the global financial architecture has become more urgent than ever.

While institutions of the post-World War II era, such as those of the Bretton Woods organisations, arguably shaped the financial landscape, their relevance in today's fast-paced world is increasingly being questioned. The current global financial system and the infrastructure created in the aftermath of chaotic conflict and industrial expansion struggle today with the complex challenges of our reality.

The Finance Track deals with strategic macroeconomic issues and is led by member countries' Finance ministers and central bank heads. There are seven technical groups in the Finance Track, as well as three Task Forces out of which the one concerning us is the International Financial Architecture.
The International Financial Architecture was established following the 2008 global financial crisis. Over the years, it has discussed policies to promote a more stable, resilient, and balanced international financial architecture.

Introduction to the topic

"Global Financial Architecture: Replacing the outdated and creating the new, creating new organisations and leveraging technology to aid Global Development." This agenda explores the knowledge of delegates in finance along with the nuances of critical and creative thinking. It requires the delegates to have deep knowledge about the historical revolutions that took place among the most important of which is the Financial Intermediary Fund. The topic also touches on topics like currency regimes and debt sustainability. The delegates are expected to have a broad idea about the institutions in the International Financial Archit ecture.

Committee Mandate

The focus of the committee will be making reforms to the current architecture and making new organisations to be a part of it. This architecture was built in the aftermath of World War II. It essentially reflects, even with some changes, the political and economic power dynamics of that time.

Because over three-quarters of today's countries were not present at the creation of the Bretton Woods institutions the World Bank and the International Monetary Fund (IMF) are concerned. Now that the world is facing an actual global issue, global warming, we also need to recognise the importance of mobilizing climate finance and incentivizing green investments.

What is the Global Finance Architecture?

The international financial architecture refers to the governance arrangements that safeguard the stability and function of the global monetary and financial systems. It has evolved, often in an ad hoc fashion, driven by the policy preferences of large economies in response to economic and financial shocks and crises. The term “non-system”[1] has sometimes been used to describe the existing set of international financial frameworks, rules, institutions and markets that together make up the international financial architecture. The international financial architecture includes:

1. Governance of public international financial institutions, such as the multilateral development banks and the International Monetary Fund (IMF), as well as other international public development banks and global funds (such as the Green Climate Fund);

2. Financial standard-setters that establish norms for the governance of private finance, such as the Financial Stability Board, the Bank for International Settlements, the International Organization of Securities Commissions, the International Accounting Standards Board and the Financial Action Task Force;
3. Monetary arrangements, such as regional financial arrangements and the network of bilateral swap lines;
4. Informal country groupings that act as norm-setters, such as the Group of Seven (G7) and Group of 20 (G20);
5. Formal but non-universal norm-setting bodies, in particular the Organisation for Economic Co-operation and Development (OECD);

6. Creditor groups that address sovereign debt issues, including the Paris Club, the London Club, the Common Framework for Debt Treatments beyond the Debt Service Suspension Initiative, agreed by G20 and Paris Club countries, and the International Capital Market Association (a private entity that publishes model clauses for debt instruments), as well as global credit rating agencies;
7. United Nations as a norm-setter and implementer.

While the international financial architecture does not include all the action areas of the Addis Ababa Action Agenda of the Third International Conference on Financing for Development, it needs to be coherent with and complemented by rules governing trade, tax, financial integrity, technology, environmental sustainability and climate action, as well as other development issues. Reforms to the international architecture (see Figure I) will have the greatest impact if accompanied by strengthened national financing policies and capacities, for example through integrated national financing frameworks, which will require significant capacity-building with support from the international community.

What is the Need for A Global Finance Architecture?

One of the main reasons for establishing the IMF was to put in place a set of international rules or guidelines that would discourage "beggar thy neighbour" exchange rate policies. After all, the world had just gone through a troublesome experience with the competitive depreciations of the 1920s and 1930s, and there was widespread agreement that the new "rules of the road" should outlaw such policies for the future.

Impact of Climate Change on Global Finance

Climate change can make banks, insurers, and reinsurers less diversified, because it can increase the likelihood or impact of events previously considered uncorrelated, such as droughts and floods. Transition risks materialize on the asset side of financial institutions, which could incur losses on exposure to firms with business models not built around the economics of low carbon emissions. Fossil fuel companies could find themselves saddled with reserves that are, in the words of Bank of England Governor Mark Carney (2015), "literally unburnable" in a world moving toward a low-carbon global economy. These firms could see their earnings decline, businesses disrupted, and funding costs increase because of policy action, technological change, and consumer and investor demands for alignment with policies to tackle climate change. Coal producers, for example, already grapple with new or expected policies curbing carbon emissions, and several large banks have pledged not to provide financing for new coal facilities.

SDG 1, 2, 3, 4:
A stable international system is a foundation of national economic growth and sustainable development. Financial shocks and crises set back progress on social goals, increasing poverty and hunger. High debt servicing can lower spending on health, education, social protection and other social priorities. Sustained economic growth is also the basis of domestic public resource mobilization, which is essential to finance public goods and services. Domestic resource mobilization also needs effective international tax cooperation to prevent tax evasion

SDG 5:
Entrenched gender biases affect the design and functioning of all aspects of the international financial system. Gender equality objectives should be part of international leadership selection and the mandates and accountability metrics of multilateral development banks.

SDG 6, 7, 8, 9:
Countries have massive investment needs to deliver infrastructure, including water, sanitation, and clean energy. A reformed international financial architecture should deliver affordable, long-term financing for such investments. Increased productive investment also drives growth and sustainable industrialization. Preventing debt and financial crises contributes to decent work and helps the financial system to sustainably expand access to financial services for all.

SDG 10:
Reforming international financial institution governance can reduce inequalities in the representation and voice of developing countries in global economic decision-making. Excessive financialization also contributes to inequality. The international financial architecture includes the standards for the regulation and monitoring of financial markets and institutions.

SDG 11:
Dedicating more finance to resiliency will reduce the losses from disasters. Investment in urban infrastructure can be boosted by the public development bank system.
SDG 12, 13, 14, 15:
Climate change and environmental sustainability need to inform all aspects of the international financial architecture. Climate- and environment-related standards and metrics should inform business, finance, investment, and financial regulation including standards set at the international level. Systemic coherence between environmental standard setting and economic management is essential.

SDG 16:
Financial integrity is a core requirement for a sustainable international financial system. Strengthening international financial integrity standards and their implementation will reduce corruption, boost trust, and enhance the social contract. A reformed international financial architecture should also provide concessional financing for conflict-affected countries.
SDG 17:
Finance issues are central to the partnerships for the goals and the means of implementation. Reforming the global tax architecture can enhance domestic revenue mobilization. Donors can channel official development assistance commitments through multilateral development banks. Reforms to the debt architecture aim at attaining long-term debt sustainability.

Supply Chain Shortages

Supply chain disruptions and the associated operational and financial risks represent the most pressing concern facing firms that compete in today's global marketplace. Extant research has not only confirmed the costly nature of supply chain disruptions but has also contributed relevant insights on such related issues as supply chain risks, vulnerability, resilience, and continuity.
Manufacturers in most industries have turned to suppliers and subcontractors who narrowly focus on just one area, and those specialists, in turn, usually have to rely on many others. Such an arrangement offers benefits: You have a lot of flexibility in what goes into your product, and you're able to incorporate the latest technology. But you are left vulnerable when you depend on a single supplier somewhere deep in your network for a crucial component or material. If that supplier produces the item in only one plant or one country, your disruption risks are even higher.
In the committee, the delegates are expected to address the issue with sincerity and come up with solutions, existing or new, to solve the issue.

Debt Trapping and its Connection with Climate

One of the biggest factors preventing governments in the Global South from taking climate action is barely discussed at conferences and debates meant to find solutions to the planet's existential crisis.
This extortionate debt which hangs over the heads of many countries is forcing them to make difficult choices to pay that debt back. Indonesia, for example, is paying back loans equivalent to more than 40 per cent of its gross domestic product (GDP), a key factor leading it to cut down rainforests to make way for money-making palm oil plantations.

The need to repay external debt worth more than 80 per cent of GDP has also been a factor in Brazil's prioritizing of soybean exports over the protection of the Amazon. And an external debt equivalent to 101 per cent of GDP is why Mozambique has been trying to expand its coal and gas production in recent years.

This type of external debt almost always needs to be repaid in US dollars or other foreign currencies. So even when countries would benefit from supporting smallholder farmers, agroecology and small and medium-sized businesses, many have been forced to shape their economies around destructive fossil fuel and large-scale industrial agribusiness exports, to earn the dollars needed for debt repayment.

The committee is expected to come up with solutions to debt trapping by forming either a new organisation or by making a drastic change to an existing one.

The Red Sea Conflict

In the past few months, global trade has been held back by disruptions at two critical shipping routes. Attacks on vessels in the Red Sea area reduced traffic through the Suez Canal, the shortest maritime route between Asia and Europe, through which about 15 per cent of global maritime trade volume normally passes. Instead, several shipping companies diverted their ships around the Cape of Good Hope. This increased delivery times by 10 days or more on average, hurting companies with limited inventories.

On the other side of the world, a severe drought at the Panama Canal has forced authorities to impose restrictions that have substantially reduced daily ship crossings since last October, slowing down maritime trade through another key chokepoint that usually accounts for about 5 per cent of global maritime trade.

The Suez Canal, through which 12% of global trade used to pass, saw traffic drop by 66% at the start of April, compared to the previous year.
Many shipping firms are now diverting vessels onto the safer, but much longer and more costly, route around the tip of southern Africa, passing the Cape of Good Hope. This can add 10 days to a journey and increase fuel costs by 40%.
The few ships that use the Red Sea route are still under threat, however. This was underlined last week when shipping line Maersk said attacks had intensified, and the risk zone was now bigger.
Maersk said it would continue to send its ships around Africa for the foreseeable future, but that this would result in a 20% drop in capacity in the second quarter of the year and additional costs. Last week, it trebled the surcharge on containers travelling between Asia and Northern Europe from $250 to $750.
For huge companies like Maersk to small businesses in the UK and elsewhere reliant on goods from Asia and the Middle East, the crisis continues to have an impact.
The committee is expected to come up with ideas on how to avoid such problems in the future and come up with effective action plans for the trade to inevitably go on despite these shortcomings.

Country Profiles

Argentina
Argentina's president criticizes the global financial system's inequity in the UN address. Alberto Fernandez said, "The global financial architecture serves only to concentrate wealth in the hands of very few,"

Australia
Australia has made attempts at improving its financial systems to improve its nation's Financial architecture and has made progress with the same.

Brazil

The first meeting of the G20 International Financial Architecture Working Group presided over by Brazil, discussed proposals to remodel the global financial order. The focus is on strengthening international financial institutions, approaching the challenges of sovereign debt, and promoting resilient capital flows.

Canada

The Canadian Bank participates in several international forums where issues of financial stability are being debated, and the bank also works closely with others to strengthen the international financial architecture by developing frameworks for the prevention, management, and resolution of crises.

China

Despite the country's growing economic weight, multilateral financial institutions have inadequately reformed their governance structure to accommodate China's demand for greater influence. As a result, China has developed its parallel financial institutions and initiatives, such as the Asian Infrastructure Investment Bank and the Belt and Road Initiative.

France

France has called for the adoption of a New Global Financing Pact (22 – 23 June 2023)

Germany

Mr. Zattler, in the 2023 session, financing for development forum, stated that World Bank reform is the most important process in town, and said Germany gives much importance to this process and has been pushing for it for years.

India

Finance Minister Nirmala Sitharaman calls for an inclusive global financial architecture that can bring countries, especially the poor and developing ones, closer to realising sustainable development goals and financing climate action.

Indonesia

Indonesia focused on bolstering the International Financial Architecture by monitoring capital flows, ensuring global financial stability, and supporting the International Monetary Fund's Integrated Policy Framework. It underscored infrastructure investment as a pivotal element for sustainable economic recovery.

Italy

Building on the works of the International Financial Architecture Working Group, the Italian Presidency also favoured a gradual shift from the provision of emergency liquidity to address the longer-term financing needs of low-income countries, while pursuing the Sustainable Development Goals.

Important Topics for discussion

Reforms in currency Regimes

Reforms in currency regimes are essential for enhancing economic stability, fostering growth, and facilitating global trade and investment. By shifting from fixed exchange rate systems to more flexible arrangements like floating or managed float systems, countries can better adapt to changing economic conditions and mitigate the impact of external shocks.

These reforms also enable nations to implement more effective monetary policies, reducing the risk of inflation volatility and speculative attacks on their currencies. Additionally, financial liberalization, which includes the removal of capital controls, promotes greater capital mobility and investment opportunities, integrating economies more deeply into the global financial system.
A notable example of such a reform is China's transition from a fixed exchange rate system to a managed float system in 2005. Previously, China pegged its currency, the yuan, to the US dollar, but the shift allowed the yuan to gradually appreciate and reflect market dynamics more accurately. This change was significant as it reduced the risk of speculative attacks and enabled a more flexible monetary policy, aiding in better inflation and economic growth management. Moreover, by allowing the yuan to appreciate, China addressed international concerns about currency manipulation and trade imbalances, promoting fairer trade practices and improving economic relations with its trading partners. This reform also attracted foreign investment by reducing exchange rate risk, showcasing how such changes can lead to a more stable and sustainable economic environment both domestically and globally.

Reforms in the current debt policies

Reforms in currency regimes are essential for enhancing economic stability, fostering growth, and facilitating global trade and investment. By shifting from fixed exchange rate systems to more flexible arrangements like floating or managed float systems, countries can better adapt to changing economic conditions and mitigate the impact of external shocks. These reforms also enable nations to implement more effective monetary policies, reducing the risk of inflation volatility and speculative attacks on their currencies. Additionally, financial liberalization, which includes the removal of capital controls, promotes greater capital mobility and investment opportunities, integrating economies more deeply into the global financial system.

A notable example of such a reform is China's transition from a fixed exchange rate system to a managed float system in 2005. Previously, China pegged its currency, the yuan, to the US dollar, but the shift allowed the yuan to gradually appreciate and reflect market dynamics more accurately. This change was significant as it reduced the risk of speculative attacks and enabled a more flexible monetary policy, aiding in better inflation and economic growth management. Moreover, by allowing the yuan to appreciate, China addressed international concerns about currency manipulation and trade imbalances, promoting fairer trade practices and improving economic relations with its trading partners. This reform also attracted foreign investment by reducing exchange rate risk, showcasing how such changes can lead to a more stable and sustainable economic environment both domestically and globally.

Making the Global Financial Architecture Suitable and Strong for the Current Time

Making the financial architecture suitable for current times is crucial for addressing contemporary economic challenges and ensuring global stability. This involves several key reforms aimed at enhancing transparency in financial systems. Strengthening regulatory frameworks to manage risks effectively and prevent financial crises is essential.

Incorporating digital innovations is also essential. Embracing fintech advancements, such as blockchain and digital currencies, can enhance efficiency, security, and accessibility in financial transactions. Additionally, promoting financial inclusion by ensuring that underserved populations have access to banking services helps in building a more equitable economic environment.

International cooperation is vital for a cohesive financial architecture. Establishing clear standards for cross-border transactions and fostering collaborative efforts to address global financial issues, such as tax evasion and money laundering, are necessary. By implementing these measures, the financial system can become more adaptive, resilient, and better at serving the needs of a rapidly changing global economy.

Appendix:

Addition of Key Milestones in Global Financial Architecture Development

To provide a deeper understanding of the evolution of the global financial architecture, it is crucial to highlight significant milestones and international efforts that have shaped the financial landscape. Below is a timeline of key events:

1940s-1960s: Post-World War II Reconstruction and Bretton Woods Institutions

- **1944**: The Bretton Woods Conference leads to the establishment of the International Monetary Fund (IMF) and the World Bank, setting the foundation for the post-war global financial system.
- **1947**: The General Agreement on Tariffs and Trade (GATT) is established to promote international trade by reducing trade barriers.
- **1961**: The Organisation for Economic Co-operation and Development (OECD) is formed, fostering economic cooperation and development among member countries.

1970s-1990s: Challenges and Reforms

- **1971**: The collapse of the Bretton Woods system as the US abandons the gold standard, leading to floating exchange rates.
- **1973-1974**: The first oil shock causes economic instability, highlighting the need for better financial coordination.
- **1982:** The Latin American debt crisis prompts reforms in international lending practices and debt management.

1997-1998: The Asian Financial Crisis exposes vulnerabilities in the global financial system, leading to the creation of new financial safety nets and regulatory frameworks.

- **2000s-Present: Globalization and Financial Crises**
- **2001**: The launch of the Doha Development Round aims to address the needs of developing countries in the global trading system.
- **2008**: The Global Financial Crisis results in significant reforms, including the establishment of the Financial Stability Board (FSB) to oversee global financial regulation.
- **2010**: The G20 becomes the primary forum for international economic cooperation, emphasizing the need for coordinated policy responses to global financial challenges.
- **2020**: The COVID-19 pandemic prompts unprecedented global financial responses, including massive fiscal stimulus packages and emergency lending facilities by the IMF and World Bank.
- **2023**: Ongoing efforts to reform the Bretton Woods institutions and address the challenges posed by climate change and digital currencies.
- Inclusion of Case Studies
- To illustrate the practical application and impact of financial architecture reforms, it is beneficial to include case studies of countries or regions that have successfully navigated financial challenges. Here are two examples:
- **Case Study 1: European Union – Financial Integration and Stability Mechanisms**
- **Background**: The European Union (EU) has developed a comprehensive financial architecture to support economic integration and stability among its member states.
- **Policies and Initiatives:**
- Eurozone Creation: The introduction of the euro in 1999 facilitates deeper economic integration and stability within the Eurozone.
- European Stability Mechanism (ESM): Established in 2012, the ESM provides financial assistance to Eurozone countries in financial distress, ensuring stability and preventing contagion.
- Banking Union: Implemented to strengthen the supervision and resolution of banks within the Eurozone, reducing systemic risks.

- **Outcomes:**
- Enhanced financial stability and resilience within the Eurozone.
- Improved coordination and response mechanisms for financial crises.
- Strengthened financial integration and market confidence.
- **Case Study 2: China – Integration into the Global Financial System**
- **Background**: China has rapidly integrated into the global financial system, becoming a significant player in international finance.
- **Policies and Initiatives:**
- Opening Up of Financial Markets: Gradual liberalization of capital markets and financial sectors to attract foreign investment.
- Belt and Road Initiative (BRI): A massive infrastructure and investment project aimed at enhancing connectivity and economic cooperation across Asia, Europe, and Africa.
- Asian Infrastructure Investment Bank (AIIB): Established in 2015 to support infrastructure development in Asia, promoting regional economic integration.
- **Outcomes**:
- Increased foreign investment and economic growth.
- Enhanced global influence and financial connectivity.
- Diversification of financial instruments and markets.

Enhanced Discussion on Challenges

- **Currency Regimes and Debt Sustainability**
- **Currency Regimes:**
- Fixed vs. Floating Exchange Rates: Discussion on the pros and cons of fixed exchange rate systems versus floating exchange rate systems.
- **Case Study:**
- **China's Managed Float System**: Transition from a fixed exchange rate to a managed float system in 2005, allowing for more flexibility and market-driven adjustments while maintaining some control over currency valuation.

- **Debt Sustainability:**
- **Challenges**: High levels of public debt, debt servicing burdens, and risks of default.
- **Solutions**: Implementing robust fiscal frameworks, improving debt transparency, and fostering international cooperation for debt restructuring.
- **Case Study:**
- Argentina's Debt Restructuring: Efforts to restructure sovereign debt and regain access to international capital markets after multiple defaults.
- Impact of Climate Change on Global Finance
- Climate Risks to Financial Stability:
- Physical Risks: Damage to assets and infrastructure from extreme weather events.
- Transition Risks: Financial losses due to shifts towards a low-carbon economy, affecting industries reliant on fossil fuels.
- Case Study:
- European Central Bank's Climate Stress Tests: Implementation of stress tests to assess the impact of climate risks on financial institutions and promote resilience.
- Mobilizing Climate Finance:
- Green Bonds: Instruments to raise capital for projects with environmental benefits.
- International Initiatives: Efforts by multilateral development banks and the Green Climate Fund to finance climate mitigation and adaptation projects.
- Case Study:
- India's Green Bond Market: Growth of the green bond market to finance renewable energy and sustainable infrastructure projects.
- **Supply Chain Disruptions and Financial Stability**
- **Global Supply Chain Vulnerabilities:**
- **Causes**: Geopolitical tensions, natural disasters, pandemics, and infrastructure bottlenecks.
- **Impacts**: Increased costs, delays, and disruptions in production and trade.

- **Case Study:**
- COVID-19 Pandemic: Analysis of supply chain disruptions during the pandemic and the strategies adopted by countries and companies to mitigate impacts.

- **Strengthening Supply Chains:**
  - Diversification: Reducing reliance on single suppliers or regions.
  - Resilience Building: Enhancing infrastructure, logistics, and risk management practices.
  - **Case Study:**
    - Japan's Supply Chain Resilience Initiative: Efforts to diversify supply chains and reduce dependency on specific countries for critical components.

Bibliography:

https://press.un.org/en/2023/sgsm21855.doc.htm

https://www.un.org/sg/en/content/sg/speeches/2023-06-22/secretary-general-remarks-the-paris-summit-new-global-financing-pact

https://indonesia.un.org/sites/default/files/2023-07/our-common-agenda-policy-brief-international-finance-architecture-en.pdf

https://www.un.org/sites/un2.un.org/files/our-common-agenda-policy-brief-international-finance-architecture-en.pdf

https://www.diplomacy.edu/resource/reforms-to-the-international-financial-architecture-our-common-agenda-policy-brief-6/

https://www.piie.com/publications/chapters_preview/3802/12iie3802.pdf

Bibliography:

https://books.google.com/books?id=ep4YEAAAQBAJ

https://www.lawep.ai/services/international-financial-architecture-agenda

https://www.un.org/sites/un2.un.org/files/international-finance-architecture-and-sdgs-en.pdf/

https://onlinelibrary.wiley.com/doi/abs/10.1111/j.1540-5915.2007.00151.x

https://books.google.com/books?id=a97sDwAAQBAJ

https://www.wsws.org/en/articles/2021/09/21/dana-s21.html

https://ijirt.org/master/publishedpaper/IJIRT158256_PAPER.pdf

https://frontofficesports.com/the-supply-chain-examined/

https://www.aljazeera.com/opinions/2023/4/27/want-to-fix-the-climate-end-debt-traps/

https://www.imf.org/en/Blogs/Articles/2024/03/07/Red-Sea-Attacks-Disrupt-Global-Trade

https://unctad.org/meeting/webinar-impact-shipping-disruptions-trade-africa

https://www.inkl.com/news/as-the-red-sea-crisis-continues-pressure-on-consumer-prices-follows-in-its-wake

https://www.theguardian.com/business/article/2024/may/12/as-the-red-sea-crisis-continues-pressure-on-consumer-prices-follows-in-its-wake

Links to steer further Research

https://press.un.org/en/2023/ecosoc7118.doc.htm

https://www.g20.org/en/about-the-g20/summit-rio-2024

https://projects.worldbank.org/en/projects-operations/products-and-services/brief/financial-intermediary-fund-for-pandemic-prevention-preparedness-and-response-engagement