



THE BRETTON WOODS COMMITTEE

Can G-20 Leaders Coordinate Global Growth?

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Washington, DC

In the wake of the September G20 Pittsburgh Summit, The Bretton Woods Committee hosted a meeting on the subject “Can G-20 Leaders Coordinate Global Growth?” on November 18, 2009. The discussion took place at The International Monetary Fund in Washington, DC, and explored some of the questions and key challenges that lie ahead as world leaders strive to maintain principles and a framework designed to create strong, sustainable and balanced global growth.

Executive Director of The Bretton Woods Committee, Jim Orr, introduced the discussion with a breakdown of the timeline that countries have agreed are reasonable measures for enabling growth, and the future meetings in June and November which are to follow through on the goals set by the last summit. Nevertheless, challenges still remain, including the recent concerns regarding China’s currency policy and inability for world leaders reach a compromise. It is with this climate that the speakers on the panel addressed the following questions:

- What are some of the policies that may pose a problem, and how should they be changed?
- What are the implications to inaction, and how real are the risks?
- How can political constraints to keeping promises be overcome?
- Traditionally, major countries’ resistance to IMF advice pose a great challenge. Could the new framework fare better?
- What role should the multilateral financial institutions play in this new effort?

Reza Moghadam, Director, Strategy, Policy and Review Department at the IMF opened the discussion. Despite his initial skepticism, he attributed great success to the G20 in creating some semblance of cooperation. During the critical moments of the financial crisis, the countries acted decisively and effectively in addressing financing, action, and coordination of poor countries. He gave two reasons to explain the G20’s success.

1. The meeting brought together key global players.

2. It engaged the involvement of G-20 leaders which was especially important during the crisis. The G20 was also successful in using the Bretton Woods Institutions on other issues. He noted, however, that the crisis provided impetus for action, and its driving power is diminishing.

Ultimately, one will have to compare the future of the G-20 with its goals in order to fully judge the effectiveness of solving the issues at hand. The Pittsburgh Summit looked to coordinate strong, sustainable, and balanced growth, and it laid out a plan.

1. It set up a template where countries are to submit their policies for the next 5 years.
2. The information that countries accrue are to be grown, researched, and shared within each of the countries in which policy is to be implemented. These countries are also sharing information with each other.
3. This leads to the last point; it is through the development of these policies that countries are buying ownership into their own growth. This has the added implication of emphasizing the quality country policy submissions because it is that information that will determine future action.

The Fund's role in this circumstance is to engage and interact with the financial ministers whose role is to look at policy frameworks and to look in and across framework. One should also put similar mechanisms to use on the Economic Outlook. The fund should continue to use internal machinery to look at potential outcomes and problems for the G-20 to discuss. The role of the Fund is a facilitator, not a pusher. The ownership of solutions and recommendations is internal to the countries involved. Nevertheless, the Fund's input will be included when discussing poverty and the developing world because of the expertise the organization has in this area's policy. This is part of the reason there is such a high potential for success.

Mr. Moghadam pointed out that this is a very serious process, especially if one looks at all the leaders that are involved. Even the intermediate processes of developing information, reports, and recommendations include upper leaders in central banks and the government. The conditions for success are all there, including all the right players for correcting the global imbalance and the joint work between developed and developing countries. While it is early to pre-judge, and it is up to the leaders of the G-20, there is reason to be optimistic of future G-20 success.

(Brad Setser, Director, International Economics, National Economic Council, spoke off the record, and his comments cannot be included in this summary.)

Amar Bhattacharya, Director, Intergovernmental Group of Twenty-Four, provided a non G-20 perspective on the process of coordinating growth. While the G-20 has been extraordinarily successful in bringing a coordinated response, there are two issues.

1. Will momentum continue through the exit stage?
2. Will political will remain for longer term issues?

Dr. Bhattacharya called the architecture of the G-20 is path breaking. It demands discipline, preparation, IMF scores, and benchmarks of internal commitments all of which are checked and collectively decided. It also promises to delivery policies in ways that may now be depended to delivery, especially if one looks to the leadership of the countries involved.

The challenge will be in the exit strategy. There is an asymmetry of surplus and deficit nations. Common challenges continue in the coordination of very different countries. Private demand has not yet taken root. All of these make coordinating global growth a problem. One major problem often overlooked is maintenance of a functioning credit market which has spurred protectionist policies and has had a huge impact on fiscal policies. Exit period has the potential of creating a large influx of capital into the development world which means the appreciation of currency and the further development trade balance. This is indicative of a larger problem: recovery is taken well in G-20 nations in that economies have shifted sideways or up, but it still lags in the poorest nations.

The impact of IMF and other multilateral institutions in comparison to bilateral aid is telling that the latter does not help as much as the combined efforts of multiple nations. Rebalancing global demand will create large changes in the demand of the developing world. The big driver is investment demand. In the developing world, insipient demand reaches 8 to 12%. It is often easy to overlook demand in these nations and simply focus on the US consumer and the relationship between the US and China, but there are additional factors to the relationship. It is important not to have a world with no surplus and only deficit. It is important to look at the supply side of the equation.

With the supply side, there are three things to keep in mind.

1. Potential is moving out from the United States
2. There has been an increase in the rate of catching up and diffusion of supply as indicated by the growth in developing nations
3. Proper savings management is leading to increased investment in developing countries.

All three of these indicate new potential for growth which is important to consider in conjunction with the demand deficit.

The G-20 is new terrain for the commitments of multilateral possibility; its policies are not like the IMF and G7, and this dynamic is positive. But for legitimacy, it must also include the 172 other players in the dialogue, not just in concern for the poor, but also

for the countries that are quickly growing out of their developing status. These countries need to be included, and a mechanism must be found for direct inclusion.

Dr. Bhattacharya also highlighted the Financial Stability Board since the crisis has been a source of innovation for a working program that has reached the same importance as the IMF and World Bank. It is striking because it does have fewer numbers but nevertheless has achieved remarkable success. The evolution of the board represents a possible future track with the IMF being the apex of macro policy, but the FSB representing the micro. The Board, however, lacks legitimacy, and needs to expand, potentially helping the G-20 achieve significant reform. Multilateral organizations like the IMF and World Bank are also going to be important in roles of surveillance and support of financial reform. They are institutions that have had experience in balancing the public and private sector in both developed and developing countries. G-20 success has been admirable, but this sector does need to be engaged.

Arvind Subramanian, Senior Fellow, Peterson Institute for International Economics/Center for Global Development spoke as the dissenting opinion of the G-20, and less optimistic in the G-20 future. He listed two imbalances that exist in today's world:

1. Cyclical imbalance or the capital flow problem for emerging markets
2. Structural imbalance or the re-emergence of global current account surpluses and deficits.

Cyclical imbalance is important but requires the repudiation of what he calls the "foreign finance fetish." Structural imbalance revolves around China and its exchange rate as key, and can only be addressed as multilateral, trade issue not a macro or global imbalance issue; in terms of multilateral institutions, this means WTO, not IMF.

Cyclical Imbalance is the result of the extraordinary loose monetary policies in the US, UK, and EU. This creates a push factor in which the dollar carries trade. This causes a resurgence of capital flow to emerging markets and increases pressures on asset prices and exchange rates in the emerging markets. The push factor is likely to persist as tightening of monetary policy for an extended period of time is very unlikely. Thus, this problem of capital flow must be handled creatively, and many are asking the question, "Should policy include capital account restriction?"

This question is increasing in importance especially in light of China's exchange rates. The solution must address the issue of asset price bubbles. If China's policy persists, and its currency does not appreciate, this will lead to capital account restriction. As a whole, the IMF response to the crisis is good, but on this point, it has not changed. This is an opportunity for the IMF both intellectually and ideologically. Stigma against this vein of thought has led to other countries such as Brazil in botching its monetary policy because

of fear of market response. There is a larger belief that both domestic finance and foreign finance are good. It is this that is meant by the foreign finance fetish.

In order to move beyond this attitude, it must include the coordination of capital accounts, under the auspices of the G-7, and it must break previously held beliefs.

On the issue of Structural Imbalance, the correction of global imbalances is projected to be longer term. The IMF project, however, seems optimistic for a couple of reasons. First, oil price assumptions might be low, and second, correction is a consequence of trade collapse and will be reversed. At the heart of the Structural Imbalance problem is a policy regarding China's exchange rate.

The IMF has neither leverage nor legitimacy to persuade China to adjust its currency. Some have suggested the concept of "Chinamerica" implying that China is beyond outside influence. If China cooperates, it is because it is in its own self-interest. Dr. Subramanian identified trade as the only source of outside influence. This is an issue that affects other emerging markets and developing countries, not just larger blocs like the US-China or EU-US relations. Because trade is the only leverage countries have with China, it is an implicit assumption that the only leverage that can be exerted is from pressure by a combination of countries, both developing and developed.

Given Dr. Subramanian's analysis, this means that the role of the IMF in such issues is diminishing, and the roles of the G-20 and WTO is greatly increasing and has yet to reach full potential. The importance of addressing this policy issue has recently been underscored in President Barack Obama's latest visit to China; an indication that there is little the IMF can do, and the G-20 or WTO must explore options further. However, if the G-20 is to reach full success, there are two issues that it must address. First, it must address the question of its creation as a response to failure of legitimacy, and second, it has been effective because of the crisis, but whether the same degree of cooperation can be achieved has yet to be seen.