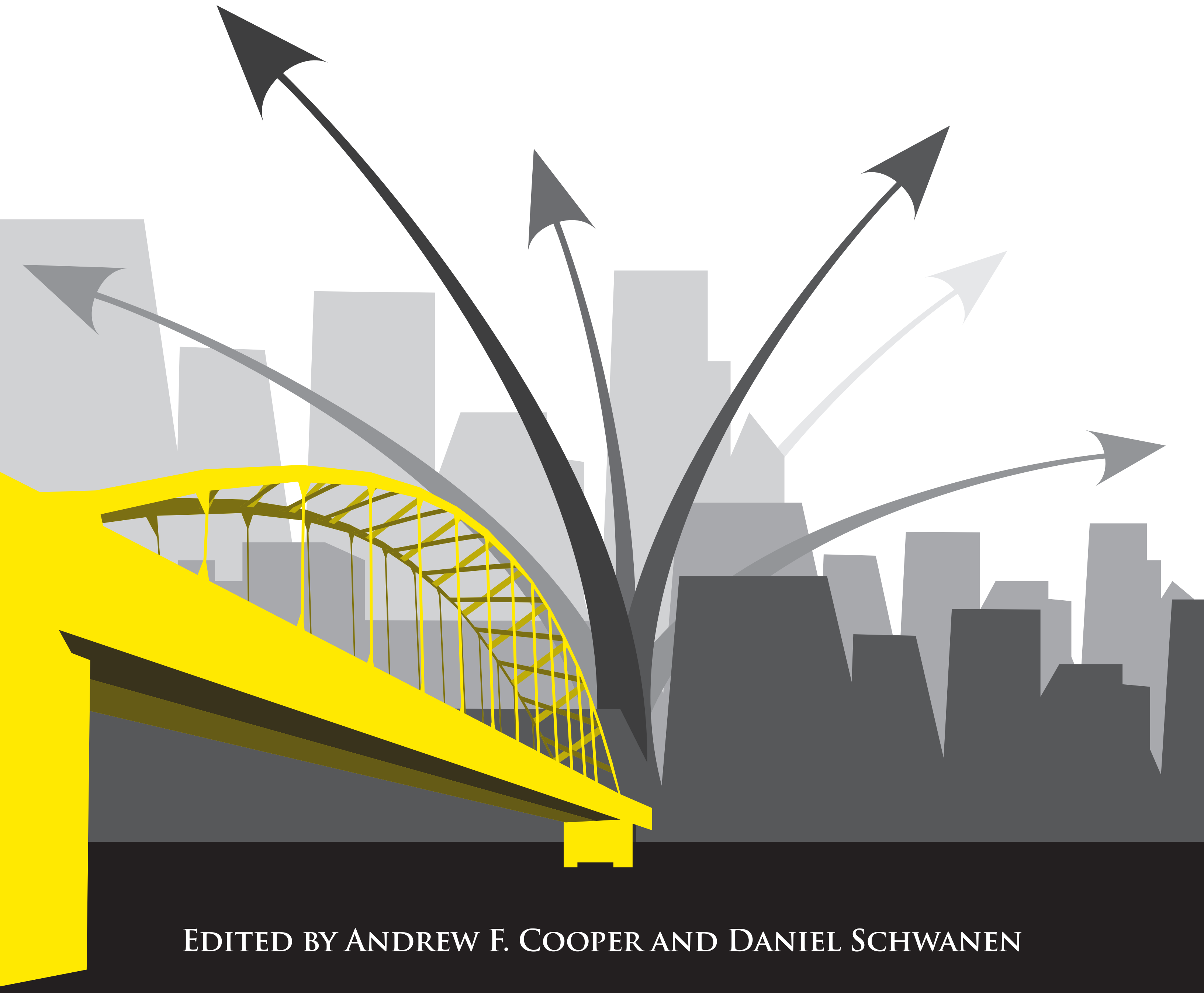
CIGI Special G20 Report:

Flashpoints for the Pittsburgh Summit

September 24-25, 2009



Edited by Andrew F. Cooper and Daniel Schwanen

CIGI
The Centre for International Governance Innovation
Centre pour l'innovation dans la gouvernance internationale

Addressing International Governance Challenges

CIGI Special G20 Report:

Flashpoints for the Pittsburgh Summit

September 24-25, 2009

Edited by Andrew F. Cooper and Daniel Schwanen

Andrew Schrumm, Assistant Editor

Table of Contents

Foreword

Jim Balsillie

Chair, The Centre for International Governance Innovation

The current global economic crisis has created an urgent need for policies that reflect innovation in governance – both regional and global – to create the institutions, mechanisms and public policies that encourage cooperation and a more cohesive world.

The Centre for International Governance Innovation (CIGI) was one of the first think tanks to recognize that the G8 needed comprehensive reform and that the world needs a more inclusive and representative forum to deal with challenges that have become global in scope and require coordinated global solutions. Since 2003, CIGI's Breaking Global Deadlocks project has convened experts from around the world in a series of topical meetings to research, discuss, provide analytical capacity and propose reform that would culminate in the first G20 Summit.

Within the past year, the G20 has become the pivotal forum for international problem solving. Brought into being as a crisis committee, it must deal with all the manifestations and aftermaths of the financial shocks. Yet, in the midst of this economic upheaval, the emergence of the G20 points to the manner by which novel ways of thinking and coordinating can be embraced. The results up to now feature many innovative components, most visible among them being big domestic stimulus packages, with promises of new resources not only for the International Monetary Fund (IMF) but also the World Bank, other Multilateral Development Banks (MDBs) and the reconfigured Financial Stability Board.

If the G20 is to pass the (stress) test of expectations going forward, the Pittsburgh Summit is key. Pledges must be monitored and turned into implementable results.

Impressive promises were made in London. These promises hinge on the delivery of resources – the London Summit resulted in the largest commitment in history to shore up the global economy through the IMF and the MDBs to the tune of US$1 trillion.

As with the pledges to deliver new resources, the G20 has also made robust commitments -- both in Washington last November and in London in April -- to stabilize the world's financial system, by regulating actors and products in the financial markets and by keeping keep borders open. The real test of these commitments remains ahead.

The implications of such reforms for global economic governance are enormous. In these pages you will find substantial ideas proposed by CIGI experts for advancing the common agenda. Having advocated and thoroughly explored the potential for an expanded leaders' forum since 2003, CIGI has proved to be ahead of the policy curve. The analysis and recommendations put forward in this publication are timely and vital. The papers assess how well the G20 has functioned as the hub of global economic governance and propose ways in which this activity can be sustained.

In detailed fashion they cover the core economic agenda items for the Pittsburgh Summit, putting forward specific policy recommendations for key stakeholders. The report also offers longer-term recommendations to consider how a new global economic compact can come into being. Although it's important to make the immediate fixes, there is a need to look beyond the current core agenda concerns to issues that are left off. Issues such as food security, development, fragile states and energy security present long-term challenges to the international system.

Out of this crisis comes ample opportunities to shape the agenda and to be at the centre of the creation of a new system of global governance.

Introduction and Summary of Recommendations

Andrew F. Cooper and Daniel Schwanen

On September 24-25, 2009, the leaders of the G20 countries will assemble in Pittsburgh to address the reverberating effects of the global economic crisis. Credible action is needed at Pittsburgh on core economic concerns, to sustain momentum on regulatory reform and to strengthen our collective ability to avert future crises.

As this compendium of brief policy papers by fellows and other experts associated with The Centre for International Governance Innovation (CIGI) examines, the G20 faces a significant challenge to reboot the world economy and restructure the global financial system. The articles in this report identify a set of flashpoints for the Pittsburgh Summit. At this critical juncture, the G20 must work to:

- Reduce the gap between declaration and action on financial regulatory issues, on reform of the international financial institutions and on trade;
- Avoid hidden dangers in the winding down of national stimulus programs, by thinking through exit strategies to ensure they do not compromise sustainable economic growth; and
- Decrease systemic risks, by improving communications and knowledge sharing among global and national markets and regulators.

Functioning largely as a crisis committee, the G20 has been tasked to generate order from chaos, to work within the international system to create new arrangements for global governance and to resolve core economic problems in recessionary times. So far, the G20 has delivered, at least in a declaratory fashion; now, it needs to put lofty declarations into action. In effect, it needs to work itself out of its first major job by reconfiguring the global economic architecture to strengthen long-term anticipatory governance processes.

Core Economic Concerns

The G20 countries have taken steps to backstop financial markets and institutions, facilitate ongoing lending and create common policy responses that likely have reduced the depth and scope of the economic crisis. Most G20 economies have begun to stabilize, while some have even witnessed a reversal of decline. Looking ahead to the Pittsburgh Summit, however, dangerous structural shoals remain below the apparent immediate success of mass infusions of stimulus funds that could still upset the economic recovery or even lead to a recurrence if left uncharted. Indeed, the challenge at Pittsburgh will be to determine which areas still need a steady hand at the tiller and which others present a unique opportunity for important new reforms or corrective actions. And beyond the immediate economic crisis, discussions should begin on the future of global summitry itself.

Mechanisms for Compliance and Accountability

The immediate test for the G20 relates to international regulatory reform. Reaching a consensus on the incorporation of macro-prudential concerns about systemwide risks into international regulation has been one of the most significant accomplishments of the G20 summits. As articles in this report note, however, there has been much slippage between G20 declarations and actual implementation. On the international reform of financial regulation, for example, the window of opportunity to act is closing. In the absence of an overarching supranational institution with the capacity to enforce international agreements – which is probably not in the cards – implementation of key systemic reforms is left to a credible form of "networked governance," which the G20 should take pains to reinforce.

The challenge at Pittsburgh will be to determine which areas still need a steady hand at the tiller and which others present a unique opportunity for important new reforms or corrective actions.

In terms of a detailed, forward-looking agenda, one form of countercyclical regulation that needs attention is agreement on clear and automatic rules by which banks can adjust buffers, thereby preventing a weakening of regulators' resolve at different stages in the economic cycle. Related questions of the appropriate division of home and host country responsibilities for bank regulation need to receive more attention, as recent events appear to have strengthened the case for host country regulation and responsibility. Key international regulatory bodies, notably the Financial Stability Board (FSB) and the Bank for International Settlements (BIS), have been charged with reporting on the development of macro-prudential modes of regulation as part of the Pittsburgh process; if these bodies were to produce an acceptable breakthrough, the G20 should move quickly toward implementation within clear deadlines.

That still leaves open the question of how to regulate systemically important financial institutions, markets and products. Despite statements by the G20 at previous summits that no such entities would escape supervision, many were treated leniently under the Basel II accord on banking laws and regulation. Here, confidence-building measures could be aided if new financial products were registered with and evaluated by a consumer financial products regulator for the risks they might pose.

Digging deeper into national responses to the financial crisis, the actions of central banks are highly salient. As in the case of financial regulation, very different regimes likely will persist, even though a fairly universal belief in low and stable inflation as well as financial stability has taken hold. These differences are not a bad thing, as policy can be delivered in a variety of forms suited to particular economies or regions. So far, however, the G20 has emphasized the sharing of information and greater transparency rather than concrete forms of joint action.

As central banks have been obliged to take truly extraordinary measures, questions have arisen as to their compatibility with the banks' long-term independence and belief in the benefits of low inflation. To quell such concerns, central banks should have guidelines on how to react in crisis situations, with specific attention to the need for fiscal authorities to be financially accountable and to highlight the limits of their responsibilities. The macro-prudential monitoring role of central banks in relation to that of other institutions should also be made more explicit, while reform efforts should be concentrated on governance issues.

Restructuring World Economic Leadership

The G20 is an important step toward the restructuring of world economic leadership. With equal status given to industrialized and emerging economies from the outset, its efforts to adapt institutions to shifting global economic power have been credible and have launched a process of reform. With the creation of a stronger FSB, which includes the G20 countries, questions of legitimacy as well as of efficiency again intrude. As in the G20 writ large, a form of networked governance should be seen as the best model. As one illustration of the application of this approach, the FSB peer review process could include at least some reviewers from outside the financial policy area.

One of the many paradoxes of the international financial crisis is the role of the International Monetary Fund (IMF). On the one hand, the IMF, with its outdated power structure, is seen as part of the problem in global economic governance. On the other hand, the G20 has been instrumental in greatly increasing the IMF's lending capacity, hand-in-hand with which have been the introduction of a number of innovative techniques, particularly the use of securities denominated in Special Drawing Rights (SDRs). Over time, the use of these securities could bolster the idea of an international reserve currency denominated in SDRs.

Beyond a myriad of other technical issues, there is the core question of whether the spirit of reform embodied in the G20 will reverberate through the IMF and, indeed, other international institutions. One of the main reasons many capital-surplus countries have not invested funds in the IMF is their perceived alienation from real IMF decision-making power. Major economies such as China and Saudi Arabia remain reluctant to infuse more capital into the IMF without a proportional increase to their quotas. For this reason, the G20 needs to encourage a more flexible governance structure that mirrors the changes in the economic and financial system, with an eye to expediting the general review of IMF quotas in 2011.

Responding to the Outlying Agenda

While the G20 has addressed many economic concerns that are at the forefront of debate, there exist many outlying issues that threaten to reverse the progress made. Turning to the contest about fiscal stimulus, the main image has been one of tensions between the Anglo-Americans (who are pushing for more discretionary fiscal stimulus through new measures) and the Europeans (who are resisting such a kick-start to aggregate demand, preferring instead to rely on automatic stabilizers such as unemployment benefits). This image has detracted from the truly remarkable size of the overall support to spending provided in G20 countries by both discretionary action and automatic stabilizers – amounting to some US$5 trillion.

It is crucial that the Pittsburgh Summit avoid rocking the boat on current stimulus measures. The next G20 declaration should recognize the value of both discretionary fiscal actions and expenditures triggered by automatic stabilizers located in the policy tool kit. Pittsburgh will be a pivotal moment in many respects, but perhaps not the time to form a definitive judgement about the recovery path. Any strategy to leave fiscal stimulus efforts behind should be careful not to trigger another dip in world economic confidence and growth.

The financial and fiscal dimensions of the crisis have received considerable attention, but its implications for trade have been less prominent. Yet, on the road to Pittsburgh, it is clear that world trade has substantially weakened, that a satisfactory conclusion to the Doha Round through the World Trade Organization (WTO) remains very much in doubt and that, beyond the issues addressed in the Round, trade and investment restrictions embedded in various new public spending measures constitute an immediate threat to the recovery of global trade. The problem is no longer tariffs but bailouts, subsidies and domestic "buy" provisions that run counter to "standstill" pledges on protectionist measures made and reinforced at the first two G20 leaders' summits. These domestic urges must be fought where possible, even if it means quickly concluding a minimalist Round in order to turn attention to these new and pressing issues.

Some have invoked the large macro-imbalances that inevitably appear from time to time as a major contributing element of the current crisis. Yet the G20 has left the issue largely untouched, mainly because of the political sensitivity attached to it. This is especially so in the case of China, which often considers concern about imbalances as criticism of its exchange rate and trade policy. Significantly, when faced with such criticism, China and other large developing economies respond by questioning the validity of the global currency framework. Will currency diversification be raised publicly as part of the Pittsburgh process? Putting the currency issue on the agenda will induce some uncomfortable questions about the US dollar system, with reverberations in currency markets. However, if a new consensus could be forged on international currencies, the benefits could outweigh the risks.

Another important gap in the G20's agenda is its response to the role communications technology has played in the international financial crisis. If macro-prudential supervision is to be effective, this gap needs to be filled, with technology facilitating both communications and new regulatory processes networked around the globe and operating in real time. To this end, the G20 should add a working group on technology.

The Longer-Term Governance Structure

The economic crisis of 2008-2009 has provided the first real test for the G20. Its original creation, as a network of Finance Ministers and Central Bank Governors in the wake of the 1997-98 Asian financial crisis, was intended to provide forward-looking, high-level consultation and information exchange among systemically important countries. Without the initial G20 finance architecture, a coordinated emergency response to the current crisis would not have been possible. In this sense, the G20 appears to be making the grade, while its successes signal the need for wider reform to realign financial and economic systems to reflect the new global realities.

Changing the "Club"

The G20 format enjoys clear advantages over the established G8 format, advantages that were particularly evident in the wake of the L'Aquila Summit, where the Italian hosts stretched the notions of "variable geometry." The G20 process takes the positive features developed through G8 summitry (the personal engagement of leaders, detailed preparation by sherpas) and expands them to provide equal status for big emergent states from the global South. Moreover, the putative deficiencies can be managed by some further refinement. One way forward is to have a rotational G20 Secretariat established through an informal management group of three consecutive host countries. Another, bolder step is to pare the G20 down to a more manageable G13 or G14, with strong participation by the emerging economic powers.

As it currently stands, the G20 summit is a classic club with a self-selected and exclusive (albeit expanded) membership, which invites criticism from the excluded. The imperatives of consultation with non-members are high. If the G20 is to build on its initial successes, it must complement its club composition with some elements of a networked approach, with connections to non-member countries together with key business, civil society and think tank constituents. The ongoing credibility of the G20 depends as well on a new monitoring arrangement that reports on progress in member countries and ensures coherence in policy implementation.

The ongoing credibility of the G20 depends as well on a new monitoring arrangement that reports on progress in member countries and ensures coherence in policy implementation.

At the same time, the IMF and World Bank were called into action before critical governance reforms could be undertaken, impeding effective responses at a time of crisis. Both institutions were poorly equipped to respond to the macroeconomic crisis in developing countries, relying too much on cautionary practices designed to limit risks to the institution at the cost of their needy developing country members. Where the existence of a crisis-ready G20 reduced the immediate spread of the global economic downturn, such innovative governance was not in place to protect developing countries. Reform, then, of the IMF and World Bank is even more crucial as the effects of the crisis deepen.

Challenging Ideational Patterns

While the core concerns dominate the work of the G20, the longer-term implications of the crisis cannot be ignored. The linkages developed through the G20 via the sharing of information, advice and assistance send a positive signal about the possibilities of joint action. But success is far from complete in terms of the level of mutually supportive policy responses and the development of a more resilient international framework. Social capital and strong social and institutional contexts provide an evolutionary advantage, allowing longer-term perspectives to be adopted. Indeed, the G20 itself is an important form of international social capital, as vital for the connections it builds as for the specific policies it is counted on to deliver.

The crisis has reflected a sudden shift in behaviour of a highly complex system that is under extreme and steadily rising stress. Abrupt flips from one condition to another require wholesale shifts in policy orientation, as they often preclude the system's returning to its previous state, leading to the breaking of long-term expectations and relationships. We now need a better understanding of the implications of complex system behaviour for public policy and governance. Policy makers should recognize that, in a system with the potential to flip its behaviour, past and current trends are not good indicators of future states. In circumstances where uncertainty and lags shroud future outcomes, yet where a wrong decision could produce catastrophic and irreversible costs, policy makers should adopt a

Recommendations: Strengthening Economic Governance

At the Pittsburgh Summit, the G20 must:

- Act quickly to deliver on past summit commitments and reduce gaps between declaration and action on the core economic and structural concerns.
- Immediately address capital and liquidity requirements, and other facets of the regulation of systemically important institutions, markets and products.
- Prioritize the introduction of macro-prudential regulation, and promptly execute the recommendations of the FSB and BIS reports. Clear and automatic rules by which banks can adjust buffers are needed to enhance the regulatory toolbox at all stages of the economic cycle.
- Promote a highly cautious approach to "exit strategies" from fiscal stimulus programs, and work toward a collective judgement on whether the expansionary fiscal actions taken thus far are sufficient, insufficient or excessive.
- Acknowledge both discretionary fiscal actions and expenditures triggered by automatic stabilizers in its accounting of fiscal efforts by G20 countries.
- Publicly recognize the failures of G20 countries to adhere to the standstill commitment on trade and investment restrictions. Tangible efforts towards ensuring an open global economy are still needed.
- Firmly commit to conclude the Doha Round by early 2010, if necessary at the price of settling for even the smallest of agreements possible.
- Define how central banks should react in crisis situations and support national legislation on the limits of central bank responsibilities. Such guidelines should underscore not only the role of government in these situations, but the need for the fiscal authorities to be financially accountable for any extraordinary liquidity/credit measures taken under such circumstances.
- Encourage flexible and more representative structures in institutions of economic governance that can more accurately reflect the current distribution of global economic power.
- Continue to act as a crisis committee, through its working groups, ministerial and leader summits, in the short to medium-term, and promote and monitor progress toward resolution of its core economic concerns.

precautionary or prudential approach to system governance. Again, in this context, the G20 should aim to avoid the effects of groupthink by becoming a legitimate and effective hub of interaction between actors that, while rooted in diverse systems, recognize the need to enhance the common well-being and to defuse the systemic risks that arise from these interactions.

Recommendations: Adapting to New Realities

At the Pittsburgh Summit, the G20 must:

- Consolidate its role as the hub of global economic governance.
- Deliver on its commitment to review the mandates and to reform the decision-making, negotiation and management structures of the IMF and World Bank.
- Set clear deadlines for IMF quota and voice reforms, particularly to expedite its general review of quotas in 2011. Emerging economies must be included in the IMF's strategic directorate, while a wider group of countries should consult on the appointment of IMF senior management.
- Push for better regional representation in the World Bank governance structure. The Bank's board of executive directors must enhance its representation in order to enunciate the collective purpose of members and set clear incentives for management and staff.
- Propel and oversee the development of communications technology in financial regulatory processes to reduce or eliminate systemic risk.
- Continue to encourage capital-surplus countries – such as China and Saudi Arabia – to commit more funds to the IMF over the medium term. Follow-up will be needed in the form of proportional increases in IMF quotas for major contributors.
- Agree to study the issue of an SDR-denominated international reserve currency, based on the concrete example of the IMF's SDR-denominated securities.
- Encourage positions on exchange rates and global macro-imbalances that consider national and systemic needs, equally.
- Build on its potential as a generator of international social capital to address complex global challenges, such as climate change, that are characterized by long-term lags.
- Develop an organizational committee, or Secretariat, that could include a troika of sherpas from the three consecutive host countries, jointly responsible for preparing summits and consulting stakeholders.

A Defining Moment

The G20 leaders' personal engagement, combined with the group's momentum, offers the prospect of a grand bargain with implications for a fundamental redesign of the governance structure of the global economy. Though deleterious, the financial crisis provides an opportunity to think and act on an ambitious scale. At its core, this vision must be directed to getting international economic organizations to work more effectively, not only on an individual basis, but also in an interconnected fashion. The current crisis shows that monetary policy affects trade and investment flows, and trade policy affects macroeconomic policy.

The Pittsburgh Summit will test both the systemic and institutional dimensions of the G20. All the momentum it has built up will ebb if it now fails to deliver in a timely and substantive fashion. The G20 is ascendant as a crisis committee, but its record and legacy are still in play. Leaders are not always comfortable with minutiae and their attention can wander back to domestic needs and interests; sherpas and other officials can become overburdened with meetings and other details, thus reducing the effectiveness of the process.

The global problems are immense, but the networked G20 approach is the best means of dealing with this complex agenda on a global basis. Pittsburgh will define whether we are moving forward or sliding backward.

The Role of the G20 in Shaping Responses to Global Crises

Barry Carin and Gordon Smith

Summary Points

- Effective follow-up and organizational mechanisms are required if the G20 is to succeed. The G20 could establish a troika, comprising the sherpas of three consecutive host countries, jointly responsible for summit preparations.
- To retain political control over agendas and implementation, a G20 Secretariat could be composed of seconded personnel from the three troika countries, on a three-year rotational basis.
- A G20 Secretariat could strengthen its role in global governance through consultative arrangements with business leaders, think tanks, academics and civil society groups sanctioned to evaluate policy options.

The leaders' G20 summit is the newest "big thing" in international relations. Looking towards Pittsburgh, the third event of its kind, expectations are once again very high. South Korea, as chair of the G20 in 2010, is already preparing for an additional leaders' summit meeting next year.

As a new informal governance arrangement, the G20 faces considerable challenges. Success is not guaranteed. In particular, the organizers must walk a tightrope between two equally demanding, but apparently incompatible, imperatives. First, personal engagement by leaders is essential. Second, extensive preparation and pre-negotiation are required given the complexity of the issues, be they severe crises or long-term policy deadlocks. Leaders' summit meetings are effective to the degree that leaders are personally engaged and the events are well prepared, if not prescribed. This difficult balancing act requires both informality and comprehensive groundwork. In effect, the hosts of a G20 summit must square a circle.

International cooperation is required to resolve major global commons problems. Progress on these global issues will require multi-element "grand bargains" — package deals with sufficient elements to allow every country to emerge a net "winner," taking all the elements into account. While consensus outcomes are ultimately adjudicated by the United Nations or other organizations with universal membership, reaching grand bargains requires a "steering group" of key heads of government. Otherwise, there will be no decision making of consequence.

Advantages of the G20

The G20 has supplanted the G8 as the major mechanism to shape consensus on critical global issues. This is certainly the case with respect to the current international financial/economic crisis. The announcement by the US that it would host the G20 in Pittsburgh effectively ensured no major decisions could be taken by the Italian-hosted G8 Summit in L'Aquila in July. In fact, at L'Aquila, the international economy was only discussed by G8 leaders in a two-hour working lunch, an arrangement in which there were not even notetakers to record any consensus that might emerge. There was another lunch to discuss "Future Sources of Growth," which included the G5 countries (Brazil, China, India, Mexico and South Africa) with the addition of Egypt. Some observers have christened this grouping the G14. To add further to the confusion in Italy, there was also a three-and-a-half-hour discussion in yet another format, the Major Economies Forum, focused on climate change but with obviously huge economic consequences. This session added Australia, Indonesia and Korea to the G8 and the G5 countries, but excluded Egypt.

The importance of personal engagement and informality (using first names, never reading statements) cannot be exaggerated. G8 leaders used to spend hours cloistered together with only their sherpas (leaders' personal representatives) present, who were located well behind their respective leader whispering on bended knee into his or (rarely) her ear. In the L'Aquila Summit, leaders of the G8-proper were only together for a two-hour working session and two meals. For the remaining two days, other leaders came and went.

Making progress on the complex technical and detailed issues on the G20 agenda will require virtuoso support for the leaders.

This is not the way to build strong interpersonal ties. Imagine the leaders of the two most populous countries in the world awaiting their turn to be ushered into the inner sanctum. The G20 keeps the same people around the table for the entire meeting. If, however, other countries continue to be added, and international institution heads and finance ministers are at the table, the requirements of personal engagement will be very difficult to achieve. Sixty around a table — even thirty around a table — does not produce intimacy. Moreover, simply having twenty leaders present for a few days will not in itself produce consensus on a global problem. Making progress on the complex, technical and detailed issues on the G20 agenda will require virtuoso support for the leaders.

Developing Compatible Frameworks

Effective preparation entails several factors; the appointment of sherpas, extensive meetings and interaction, and follow-up. The sherpas should meet several times over a six-month period in the lead-up to the summit. This practice would follow the G8 tradition. The presidency by the host country is an onerous duty, exponentially greater with twenty as compared to eight countries. In the G8 practice, the host sherpa often visits each counterpart for a face-to-face bilateral meeting early in the preparatory process. A visit after the summit to monitor follow-up would be desirable. In the G20, however, a single individual could not handle these travel requirements.

The solution for the lead sherpa lies in a variation of European Union (EU) and Association of Petroleum Exporting Countries (APEC) practices. The G20 could establish a troika, with the sherpas of three consecutive host countries jointly responsible for heading a Secretariat to prepare for the summits, sifting through policy ideas and pre-negotiating potential commitments. The APEC Secretariat includes a deputy executive secretary (read: sherpa) from the following year's host country.

When a nation becomes the host country, its deputy becomes the executive secretary.

In the G20 format, an independent permanent secretariat is a non-starter. Political control is imperative. Leaders will not delegate authority to an independent permanent bureaucracy. The G20's Secretariat could, however, be composed of seconded personnel from the three troika countries, on a three-year rotational basis. Expertise, flexibility and a range of perspectives can be provided by secondments from UN agencies, the G24 Secretariat and the OECD Secretariat, the South Centre, as well as from non-member governments.

Effective follow-up is required if the G20 is to succeed. Commitments made must be monitored. Countries must "walk the talk." If that does not happen, the G20 will fail; the main reason that will be adduced is most likely that the G20 is too large. The G20 would then be succeeded by a newly created and smaller body, larger than the G8 but smaller than the G20. The musical chair gyrations in L'Aquila noted above make this outcome more likely than less.

Prudent Global Stewardship

The closer the G20 comes to reality as a global steering committee, the greater the pressure to participate will be from those on the outside (both from countries left out and from non-governmental groups). A new effective and legitimate institutional architecture cannot be created if countries, regions or sectors believe their voices are not heard and their ideas duly considered. There are no axiomatic criteria to determine the membership of the G20. Spain and the Netherlands lobbied furiously to be included in the first two G20 leaders' meetings. Non-Europeans wonder why there are six European seats at the G8 (counting the participation of the EU presidency and the EU Commission) and why six European countries claim membership in the G20. Serious consultative arrangements will have to be established with excluded countries and with the business community, civil society and policy research community.

The argument for a troika is reinforced by the imperatives of consultation with non-member countries. Regional consultations will not suffice. There will be no escaping extensive travel by the G20 sherpas responsible for the agenda. To deal with the private sector, a Business-Industry Advisory Committee, what has been dubbed a "B20," could be established. The B20 could collect, aggregate and deliver the business viewpoint. To deal with civil society, a G20 Civil Society Advisory Committee, perhaps organized by the Conference of Non-governmental Organizations in Consultative Relationship with the United Nations (CONGO), could present the views of NGOs. To analyze complex policy issues, ensuring that every country appreciates all views, a G20 Think Tank Network could be mandated to evaluate optional approaches. The members in each country should be influential policy research institutions respected by their own governments. The activities of the network would help provide a level global playing field with respect to information on policy options and implications. The G20 could establish an Academic Council of Global Economic Institutions to provide a focal point for longer-term research.

The long-term credibility of the G20 will depend on follow-up to assure implementation of its commitments and agreements. This will require new monitoring and coordination mechanisms. The G20 Secretariat officials from the troika countries could be assisted by a new arrangement to report on progress and ensure coherence. The major international organizations could establish a standing Inter-Institution Policy Committee, which could report formally to the suite of institutions. Their reports could highlight gaps and inconsistencies that need to be resolved with respect to G20 commitments.

Conclusions

The interconnections of global issues do not respect ministerial portfolio boundaries or the mandates of sectoral international organizations. Leaders are required to confirm agendas and set directions. Yet, G20 leaders cannot resolve complex issues in one-day summit meetings; a sophisticated preparatory process is required. The challenge is to retain informality and leaders' personal engagement, but at the same time arrange negotiations of complex issues among 20 participants. It will be demanding to calibrate the status and capacity of the Secretariat that must prepare the summit. To summarize, a number of steps could be taken to develop a G20 governing framework:

- The sherpas — high-ranking officials with the confidence of and access to their respective leaders — should meet several times over a six-month period in the lead-up to the summit.
- The G20 could establish a governing troika, with the sherpas of three consecutive host countries jointly responsible for heading the Secretariat preparing the summit, sifting through policy ideas and pre-negotiating potential commitments.
- A G20 Secretariat could be composed of seconded personnel from the three troika countries, on a three-year rotational basis, supplemented by temporary secondments from UN agencies, the G24 Secretariat, the OECD Secretariat and the South Centre.
- Consultative arrangements could include:
    - A G20 Business-Industry Advisory Committee (a "B20") to collect, aggregate and deliver the business viewpoint.
    - A G20 Civil Society Advisory Committee, organized by CONGO.
    - A G20 Think Tank Network mandated to propose and evaluate optional approaches.
    - An Academic Council of Global Economic Institutions to provide a focal point for longer-term research.
- To ensure follow-up, the major international organizations could establish a standing Inter-Institution Policy Committee, to report on progress and ensure coherence.

Global issues are too complex to be resolved by the G8; by an "invisible committee" of countries; by a G2; or some other "minilateralist," self-selected, small group. The leaders'-driven G20 process is the best bet. Prospects are bright if it provides for a troika; a competent, well-resourced rotational secretariat; and appropriate consultation arrangements.

Shrinking from Duty? Tasking the International Financial Institutions

Ngaire Woods

Summary Points

- To avert worsening effects of the economic crisis, G20 countries will need to act faster to deliver what they have already recognized as necessary.
- The G20 has been distracted in regulating things that were not central to the causes of the crisis and must immediately address elements that were, including capital and liquidity requirements, credit-rating agencies, financial sector remuneration and credit default swaps.
- Lack of reform at the IMF and World Bank has impeded the ability of both institutions to deliver in a time of crisis. Urgent steps to establish more responsive and representative governance frameworks need to be supported by the G20 at Pittsburgh.

Amid tremendous popular pressure, global leaders met in Washington, in November 2008, and then in London, in April 2009, to seek collective solutions to the financial crisis. Only 10 years earlier, finance ministers from the same 20 countries responded to the East Asian financial crisis by declaring they would make globalization more inclusive and safer for all. Subsequently, they accelerated globalization, particularly in financial markets. But they failed to make it safer. Their citizens now face unemployment, foreclosures and a sharp economic slowdown. It is no surprise that so many citizens expressed anger with their governments for letting global finance veer so hopelessly out of control.

The G20 leaders have shown they can, if necessary, act together to manage the crisis; but, they seem to be shying away from key issues which involve the IMF and World Bank, which must be resolved:

- The prospects of sound financial regulation are slipping away at a scary speed.
- Promised assistance to poor developing countries looks increasingly like a mirage.
- Efforts to reform, update and strengthen the IMF and the World Bank have been half-hearted at best.

Regulating Global Finance: The Big Fish that Always Gets Away

The crisis exposed the over-leveraged banking systems of the US, the UK and elsewhere. Banks took excessive risks. Fuelled by compensation systems based on short-term profits, they outsourced due diligence to credit-rating agencies. The crisis exposed horrific gaps in regulation. Hidden from the regulators were large risk concentrations and leverage. Ignored were overall leverage and systemic risks. For this reason, the crisis required a massive public bailout of banks and huge injections of public money into major economies which haemorrhaged when global finance faltered. It was no surprise the G20 promised immediate action to strengthen regulation.

This was not the first time leaders of major economies made such promises. Recall that in the 1980s, a financial crisis exploded when the unregulated offshore lending activities of major banks proved unsustainable — with their excessive loans to Poland, Mexico, Argentina, Venezuela and a dozen or so other countries — and posed a systemic risk. Public money, the IMF and the World Bank were wheeled in to save the system from collapse. The publics in the US and Europe were assured that international banking would henceforth be regulated to avoid future bailouts. Yet very little was done and much too slowly. Subsequent financial crises have exposed yet larger risk taking, each time with more global implications.

If G20 countries dither, it will be the financial sector that ensures that the fine detail of the regulation is written so as not to affect its core profitability, regardless of whether this leaves massive systemic risks looming over the general public.

If major governments fail to regulate the global financial sector — banks, investors and insurers — in the wake of this crisis, they will have yet again doubled the moral hazard involved in financial markets. Put simply, the largest institutions taking the largest risks will know with a yet greater certainty than before that they are too big not to be bailed out.

The G20 must immediately address capital and liquidity requirements, credit-rating agencies, financial sector remuneration and credit default swaps. To date, world leaders seem to have been distracted into regulating things that were not central causes of the crisis (such as offshore tax havens). Worryingly, they are backing away from initial promises to regulate elements that were direct causes (such as compensation systems and credit default swaps). Right at the heart of regulation arguments are continuing about what new capital and liquidity requirements should be set.

The slowness of policy makers is not a good sign. If the history of regulation screams one thing, it is that the moment of political opportunity to properly regulate markets passes very quickly. As a recent study on *The Politics of Global Regulation* which I completed with Walter Mattli (Princeton University Press, 2009) demonstrates, once out of the public gaze, the complex and difficult job of writing new rules inevitably gets taken up and pressed by those with the sharpest knowledge of the industry and the most resources to influence regulation. Simply put, if G20 leaders dither, it will be the financial sector that ensures that the fine detail of regulation is written so as not to affect its core profitability, regardless of whether this leaves massive systemic risks looming over the general public.

Promising Assistance to the World's Poorest: Will it be Delivered?

The crisis has caused a "development emergency" (to quote the UN secretary general, the IMF and the World Bank). The latest Global Monitoring Report indicates that hard-won gains towards the Millennium Development Goals (MDGs) are being reversed. Some 40 percent of developing countries are highly exposed to the poverty effects of the crisis. The goal to halve world poverty by 2015 (which looked so attainable before the crisis) is quickly slipping out of sight. The Report estimates that the crisis will plunge as many as 90 million more people into poverty.

The G20 leaders said in April 2009:

> We recognise that the current crisis has a disproportionate impact on the vulnerable in the poorest countries and recognise our collective responsibility to mitigate the social impact of the crisis to minimise long-lasting damage to global potential.

They reaffirmed their aid pledges and promised new resources. Yet, beyond fast rhetoric, there is little evidence that they are in fact delivering to the poorest and neediest countries. The IMF has worked fast to lend to countries in crisis. It has made 18 new loans since the crisis began. However, some 68 percent of this amount has been lent to three countries: Romania, the Ukraine and Hungary. Add to these the other European countries Serbia, Belarus, Latvia and Iceland, and one finds that more than 82 percent of the total was pledged to European countries. By contrast, just 1.6 percent of new lending has been to countries in Africa.

- The World Bank's contribution to managing the crisis is being achieved with very few additional resources, in spite of G20 rhetoric. Although the Bank's President Robert Zoellick has called for industrialized countries to pledge 0.7 percent of their stimulus packages to a new Vulnerability Fund for developing countries, his request has been largely ignored. Instead, the Bank is being forced to repackage its International Bank for Reconstruction and Development (IBRD) and International Development Association (IDA) loans, such as front-loading commitments. One result is that the Bank is unable to respond to a number of countries rendered particularly vulnerable by the crisis, but which fit neither the IBRD nor the IDA eligibility criteria or allocation models. A second result is that countries benefiting from front-loading are being forced to take a big gamble on a swift global recovery, for having accessed these resources early, fewer resources will be available later.
- The rich countries' financial crisis has created a tsunami which is overwhelming developing countries; which will reverse gains made towards the MDGs; and may well create new failed states where terrorism, drug and people trafficking, and piracy can flourish. The G20 have clear self-interests in averting this eventuality, but they will need to act faster to deliver what they have already recognized is necessary.

A More Responsive IMF and World Bank?

Are the IMF, World Bank and other global aid institutions properly equipped to deal with the crisis? Prior to the crisis it was widely accepted that the IMF's governance, mandate and financial structure all needed overhauling to enhance the institution's relevance, legitimacy and effectiveness. A similar debate has surged forward in the World Bank. Analyzed closely, it would seem that unreformed governance is impeding each institution.

Monitoring and surveillance have been put at the top of the G20's list for the IMF, yet the Fund does not have the authority required for such duties. In the past, when powerful members called on the IMF to conduct "tougher surveillance" (sometimes a codeword for pressuring China to appreciate its currency) and financial sector assessments, they have not all been so keen on allowing the IMF to apply these rules to themselves (the US has been extremely reluctant to permit a financial sector assessment of itself). New tough rules which apply to all countries will need to be accepted not just among the G7, but by powerful emerging economies such as China, India and Brazil. They will only agree if they believe the institution will be even-handed and impartial in its application of the rules. The failure to reform the IMF after the East Asian financial crisis of 1997 led these countries to amass foreign exchange reserves as "self-insurance" or "financial independence" from the IMF. Reversing this practice would require reforms which credibly signal change.

To date, the G20 has simply rubberstamped the very modest package of reforms to chairs and shares which were established pre-crisis. These increase the small voting shares, mostly of South Korea, Singapore, Turkey, China, India, Brazil and Mexico. They have not led to any willingness on the part of China, Brazil or India to participate in extensions of large credit lines to the IMF to deal with the crisis. At a minimum, governance reform to this end would need to:

- Include emerging economies in the strategic directorate which makes decisions about the role and direction of the IMF (until now, essentially the G7);
- Permit a wider group of countries to appoint and hold to account the senior management team of the IMF; and,
- Reduce the special majority required for key decisions (or, less diplomatically put, suppress the US veto) and extend efforts to inform and persuade legislators and political representatives beyond Washington to other capitals across the world.

The poorer countries have been left out in the cold in response to the crisis. IMF lending reflects the extent to which the institution's resources and mandate are used by a small group of its shareholders to manage their highest priority and most immediate concerns. New instruments, more money and less conditionality have been swiftly provided for Europe's immediate neighbours. Low-income countries, by contrast, were told by the IMF in June 2009 that they can expect it to provide "only around 2% of low-income countries' (gross) external financing needs."

The IMF's governance structure leaves it poorly equipped to respond to the macroeconomic crisis in poor developing countries. These countries play almost no role in holding the institution and its staff to account, in setting its priorities, or even as subjects of the research and expertise of the institution. The addition of two alternate directors to assist in the representation of African countries will achieve little unless there are stronger concrete incentives for other board members, management and staff of the IMF to heed these representatives — and unless the representatives themselves are held to account by the countries they represent. Greater transparency of the Board and measures to create an incentive for rich and powerful members to consult with the numerous but voting-power-poor countries (such as requiring a majority of country votes for decisions) could begin to change this.

The World Bank's response to the crisis highlights the extent to which the Bank is locked into a governance structure that has evolved to minimize risks to the institution, at the cost of its needy developing country members. In theory, the Bank has two capacities vital to managing this global economic crisis: coordinating wealthy countries' donations and responses to emergencies; and mediating loans from capital markets when private lenders shy away from the risk of lending directly to developing countries. These could be more effectively deployed if richer countries took more risk on their own shoulders.

The Bank's response has been impeded by a multi-layered system developed by the Board and management to minimize potential financial and reputational risks to the agency and its wealthy members. The result is a Bank too slow, too risk averse and too unresponsive to its needy members to be as effective as it can and should be.

To deliver urgent assistance in a crisis, the World Bank needs a Board that articulates the collective purpose of members and sets clear incentives for management and staff to deliver on its promises. The governments sitting on the Board need to make decisions to give the institution "political cover," with major governments themselves collectively shouldering risks, permitting the Bank to act rapidly in uncharted terrain and to act with other international institutions without fearing damage to its own procedures and rules (consider for a moment the way the G7 directed the IMF at times to take large risks in response to Russia or Argentina). The Board must be small enough to be a directorate, yet representative enough to be effective. It needs input from different regions and countries, in part to be better informed, in part to mobilize resources, and yet, more importantly, because if countries do not feel represented in the organization, they can simply refuse to "let the Bank in." The latter would directly erode the institution's capacity to deliver results in response to a crisis or in respect of other global public goods, such as climate change.

A new Bank governance structure could comprise a strategic directorate of representatives from each of the major regions: North America, Central and South America, Asia-Pacific, Africa, Middle East, the European Union, Russia, and non-EU Central and Eastern Europe. It could complement and reinforce, rather than dominate and control, the regional development banks across the major regions.

Crisis as Catalyst to Redesign the International Economic Architecture

Debra P. Steger

Summary Points

- Economic solutions cannot be developed in separate silos; finance and trade officials need to work together to ensure policy coherence and guard against conflicts.
- A more comprehensive blueprint for reform is necessary, including a review of the respective mandates of the IMF, World Bank and WTO.
- Greater cooperation is needed among the international economic organizations, particularly at the staff level, in carrying out their research, surveillance and advisory functions.

In the final communiqué of the London Summit, G20 leaders affirmed their belief that "the only sure foundation for sustainable globalisation and rising prosperity for all is an open world economy based on market principles, effective regulation, and strong global institutions."

At this critical juncture, the world needs a bold vision for redesigning the international organizations responsible for the global economy. In the 1940s, the Bretton Woods system was the brainchild of great minds: John Maynard Keynes and Harry Dexter White. Coming out of the Great Depression and the Second World War, leaders were determined not to repeat the mistakes of the interwar period, and charted a new course of global cooperation by creating international organizations to ensure economic prosperity and maintain peace. The original Bretton Woods organizations — the International Monetary Fund (IMF), the International Bank for Reconstruction and Development (the World Bank) and the International Trade Organization (ITO) — were designed to work together as a system, each with its own mandate and governance structure.

The financial crisis has highlighted once again that international cooperation is needed to resolve serious global problems. It has also demonstrated that more regulation of the international economic system is required, not less. The time has clearly come for a bold vision of a new global architecture — a redesign of the international economic organizations — reflecting that the world has changed since the 1940s when these international organizations were first created. The United States and Europe are no longer the only major powers on the world stage, as the emerging economies — led by China and India — play increasingly important roles. Globalization has connected states, corporations and civil society in ways never before seen. Global problems require global solutions; strong international institutions are needed to implement commitments.

Roles for the G20, Governments and International Organizations

The G20 is an important new institution involving the leaders of a diverse group of countries, reflecting the realities of the new power relationships in the world economy. The G20 leaders can provide essential policy direction to steer the international economy on a steady course through turbulent waters. However, their policy commitments will need to be implemented domestically by governments and globally by international organizations. As leaders have emphasized, strong global institutions are necessary to carry out their policy directions.

The existing rules, decision-making procedures, management structures and surveillance mechanisms were created for a much smaller and less complex world with different issues.

A concerted global effort is needed to reform the regulatory and surveillance mechanisms at the international level. While much needs to be done by national governments to improve regulatory frameworks, there are limits to what can be done at the national level. There are also important rule-making and surveillance roles for international financial institutions.

Beyond Incremental Reform

The statements of G20 leaders to date go part of the way but not far enough. At the London Summit, leaders agreed to increase the IMF's resources, in particular, and to reform the IMF and World Bank. However, their commitments were focused on incremental reform, not a complete overhaul of the existing organizations. A more comprehensive blueprint for reform is necessary, including a review of the respective mandates of all three international economic organizations (IEOs): the IMF, World Bank and WTO. The IEOs must be redesigned with stronger governance structures, and made more accountable, representative and effective in order to equip them for the challenges of the next 20 years, beyond the current crisis.

As presently constituted, the IEOs do not have the necessary mandates or governance structures to respond to the challenges ahead. Worse, the existing rules, decision-making procedures, management structures and surveillance mechanisms were created for a much smaller and less complex world with different issues. A bold, courageous vision is called for; incremental reform will not address the serious legitimacy concerns, problems in representativeness and accountability, and deficiencies in mandates of the existing international organizations.

Policy Coherence and Increased Resources for International Organizations

Monetary policy impacts trade and investment flows, and trade policy impacts macroeconomic policy. In the age of globalization, issues are interconnected. Policy responses to modern global challenges, such as climate change, have implications for both the international trade and finance regimes. Solutions cannot be developed in separate silos; finance and trade officials need to work together to ensure policy coherence and guard against conflicts. There is an important role for strong international organizations that can study the long-term effects and conduct surveillance of national policies, as well as provide negotiating forums for new international rules and dispute resolution in a fair and transparent manner.

At both the national and international levels, there is a lack of coordination on trade and finance policies, creating risks of policy incoherence and the potential for conflicts. Better cooperation and collaboration among the staffs of the IEOs is necessary to ensure greater coherence in international economic policy.

Additional resources are woefully needed by the IEOs, the WTO in particular, in order to carry out their important functions. On surveillance, the WTO has developed an excellent model in the Trade Policy Review Mechanism, which is now being applied to new preferential trade agreements. However, the WTO has very limited resources for this important work. While the WTO Secretariat relies extensively on the surveillance reports of the IMF, the same is not true for the IMF. Greater cooperation is needed among the staffs of the IEOs to carry out their research, surveillance and advisory functions. In the WTO, all member countries are subject to multilateral surveillance; however, in the IMF, surveillance is carried out only for debtor countries. In order to prevent future crises, all members of the IMF should agree to subject themselves to surveillance of their monetary and fiscal policies.

The Consequences of Inaction

A major short-term priority is concluding the Doha Round. There will be tremendous benefits for the global economy, especially for developing countries, from the reduction of trade barriers and increased market access. Moreover, the Doha Round difficulties have paralyzed the WTO, making it incapable of moving ahead with a new economic agenda for the challenges of the future.

If the IEOs are not redesigned to update their mandates and governance structures, their legitimacy and effectiveness will diminish, and other institutions or regional alliances may take their place. In order to meet the serious challenges of the future, the IEOs may be overburdened with duties and responsibilities beyond their current mandates and capabilities. Without greater cooperation and coherence, serious conflicts could arise in areas such as currency valuation and climate change.

If the Doha Round is not concluded soon, there is a real risk the WTO will become increasingly irrelevant as the proliferation in preferential trade agreements continues unabated.

The financial crisis has highlighted the antiquated mandates and governance structures of the IMF and World Bank, in particular. Uncoordinated, unilateral actions on currencies or climate change could stretch the WTO dispute settlement system beyond its mandate and threaten the legitimacy of the WTO's rules-based system. The effectiveness of the IMF and the World Bank has already been called into question by the crisis.

If concerted, collective action is not taken now to strengthen these multilateral institutions, they will crumble or collapse from the weight of the new responsibilities imposed upon them, because they have neither the authority nor the procedures to deal effectively with future challenges. Proliferation of preferential trade agreements, international investment treaties and other international arrangements will continue to fragment, and threaten stability and coherence in the multilateral system.

Phoenix of a New Global Order

The IMF and World Bank are in crisis — their mandates and governance mechanisms are out of date. The WTO is in a state of paralysis. The challenge of reforming the IEOs is great, and the window of opportunity is narrow. The financial crisis has drawn sharp attention to the shortcomings of IEO governance structures. Transformational moments in history come along very rarely. This is one of those moments.

The international economic system needs to be redesigned to accommodate new realities; the mandates of the IEOs need to be examined and expanded; their decision-making structures revamped to give voice to developing countries; and their management structures reconfigured to make them more accountable, effective and efficient. All countries have tremendous stakes in the viability and effectiveness of the international economic system.

From the ashes of this global economic crisis, a phoenix could arise: a more inclusive, transparent, representative, efficient and effective international economic order that promotes global macroeconomic and financial stability, growth, sustainable development and peace. To build a robust, stable and balanced international economic order, leaders will need bold vision and courageous commitment.

In order to achieve these goals, G20 leaders should agree to:

- A bold vision to redesign the international economic architecture and strengthen the institutional governance structures of the IMF, World Bank and WTO.
- A commitment to review the mandates and reform the decision-making, negotiation and management structures not only of the IMF, but also of the WTO and the World Bank.
- A commitment of new resources to strengthen the internal management and surveillance capacities of the IMF, World Bank and WTO.
- A commitment to promote greater cooperation between finance and trade policy officials in national governments as well as among staffs of the IEOs to ensure greater coherence in international economic policy making.
- A firm commitment to conclude the Doha Round by early 2010.
- A strong commitment to resolve global problems through multilateral institutions and frameworks, wherever possible, rather than resorting to unilateral or bilateral solutions.

Make or Break Time for International Financial Regulatory Reform

Eric Helleiner

Summary Points

- The adjustment of counter-cyclical buffers should abide by clear and automatic rules, preventing private-sector lobbying from weakening regulators' resolve at different stages in the economic cycle.
- New financial products should be registered and evaluated on an ongoing basis. In a similar manner to pharmaceutical drugs, some products could be endorsed for everyone's use, others could be restricted to authorized users, still others could be available only in limited amounts to pre-screened users, while a final category could be banned outright.
- The strengthened peer review mechanism through the FSB should be mobilized right away to help address the implementation of international commitments.

The core agenda item at both the Washington and London G20 summits was international financial regulatory reform. Although the leaders made some progress in addressing weaknesses revealed by the current crisis, much more needs to be done on this topic. There is a serious risk of slippage at the implementation phase, even with respect to the limited issues that have been agreed upon. If the G20 leaders do not stay focused on an ambitious agenda, the opportunity for reform will be squandered and the world will stumble once again — fully warned and eyes wide open — into yet another major crisis in the coming years.

The Importance of Implementation

The first two G20 summits outlined some very detailed initiatives relating to the reform of international prudential regulation in areas such as banking, credit rating agencies, hedge funds, derivatives, and even pay and compensation within financial institutions. These initiatives are welcome, but it is still unclear whether the commitments made in international meetings will be implemented fully in national jurisdictions.

Unlike in the trade realm, there is no supranational institution to enforce international financial regulatory agreements. Key international regulatory bodies such as the Financial Stability Board (FSB) or the Basel Committee on Banking Supervision (BCBS) have no formal power; they simply facilitate networks of informal cooperation, information sharing and the development of international "soft law" whose implementation is left to the discretion of national authorities.

In this context, it is particularly important that G20 leaders collectively reiterate at the Pittsburgh Summit the importance and urgency of implementing the initiatives they have already backed. As the intensity of the crisis subsides, there are already signs of weakening political impetus for reform. Resurgent competitive rivalries between different national financial systems are also beginning to challenge regulatory initiatives. The risk of backsliding on commitments is heightened by the fact that the content of G20 initiatives is often ambiguous enough to allow for significant divergences at the implementation phase.

Refining Rules for Macro-Prudential Regulation

G20 policy makers also need to resolve some complicated policy issues relating to rules for implementing macro-prudential regulation. Reaching an international consensus about the need to incorporate macro-prudential concerns about system-wide risks (as opposed to the micro-prudential focus on the stability of individual institutions) into international regulation was one of the most significant accomplishments of the G20 summits. The G20 leaders have been particularly supportive of counter-cyclical regulation, which encourages banks to build up buffers in boom times that can be drawn down in busts. But they have yet to agree on the rules by which banks will adjust buffers. While some leaders favour leaving this to the discretion of regulators, others argue, more convincingly, for clear and automatic rules to help prevent private-sector lobbying from weakening regulators' resolve at different stages in the economic cycle.

The new macro-prudential focus also requires G20 policy makers to devote more attention to the appropriate division of home and host country responsibilities for bank regulation. Since credit cycles vary across countries, a strong case can be made for macro-prudential regulation to be implemented on a host country basis. Indeed, the case for greater emphasis on host country regulation more generally has been strengthened by the crisis, which has dramatically revealed that fiscal support for financial institutions is ultimately national. Requiring foreign banks to establish local subsidiaries backed by local capital is one obvious response to this political reality. Whatever the costs and benefits associated with greater host country control, the issue of allocating responsibility for macro-prudential regulation in particular must be resolved soon.

At the London Summit, G20 leaders called on the FSB, the Bank for International Settlements (BIS) and international standards setters to report on the development of macro-prudential tools by this autumn. If these and other issues relating to the introduction of macro-prudential regulation are thoroughly addressed by these bodies, the G20 leaders should quickly establish clear deadlines for implementation.

What Should Be Done About Systemically Important Entities?

Policy makers have also yet to tackle in a comprehensive way one of the most important regulatory questions: how are systematically important institutions, markets and products to be regulated? The G20 leaders have previously declared decisively that no entity of this kind would escape regulation and supervision in the future. This decision provided the justification for extending regulation to new areas such as hedge funds and derivatives, but policy makers have yet to explain how regulators will draw a boundary between what is and what is not systematically important as well as how the former should be treated differently than the latter.

The most urgent (and controversial) issue concerns the treatment of systematically important institutions. Emerging from the bailouts, mergers and acquisitions associated with the crisis are a set of even larger and more interconnected financial institutions. These institutions are also more aware than ever that they are backed by the implicit state support because of their systemically significant status, an awareness which may encourage them to resume excessively risky activities. Clear policy needs to be developed quickly about the treatment of these financial giants.

One policy response would be simply to break up these institutions in order to ensure that no financial institution is too big or too interconnected to fail. Alternatively, these institutions could be restricted from high-risk activities and forced to act more like public utilities. A third option would be to subject these institutions to tougher standards (for example, capital, leverage, liquidity, compensation) and to require them to prepare a "will" or "funeral plan" which outlines how they would be wound down in the event of trouble.

While each of these options has its merits, the third seems most likely to be embraced at the international level at the moment. Regardless of the choice, these proposals all have in common the goal of curtailing or penalizing systemically important institutions. Before the crisis, the largest banks experienced the opposite treatment; under Basel II, they had laxer standards because of policy makers' trust in their sophistication. Reversing this mistake is one of the most important pieces of unfinished business on the current reform agenda.

Given recent experiences, it would also be wise to embrace a more precautionary stance with respect to potentially systemically important markets and products. The crisis has highlighted the systemic risks that can be associated with unregulated over-the-counter markets. Requiring the use of central counterparties for clearing and/or exchange trading will reduce these risks and enable supervisory oversight and regulatory intervention when necessary (including for macro-prudential reasons).

In a similar precautionary spirit, the BIS and others have recommended that all new financial products be registered and evaluated on an ongoing basis by a consumer financial products regulator for the systemic risks they might pose. Like pharmaceutical drugs, some products could be endorsed for everyone's use (like over-the-counter drugs), others could be restricted to authorized users (like prescription drugs), still others could be available only in limited amounts to pre-screened users (like drugs on experimental trials), while a final category could be banned. Products could also change their status over time as experience taught regulators more about them. Such a system would help officials to evaluate and regulate products such as credit default swaps — which caused so much havoc in this crisis — in a more comprehensive and nuanced way.

Widening the Accountability of International Regulatory Bodies

The final piece of unfinished business relates to the governance of international financial regulation. The G20 leaders have devoted considerable attention to strengthening governance by transforming the weak Financial Stability Forum (FSF) into a stronger FSB. The latter has been assigned a full-time secretary general and important new functions relating to early warning exercises, mandatory peer reviews for members, strategic reviews of the work of international standard-setting bodies, and the creation of supervisory colleges for all major cross-border financial institutions.

These initiatives are dismissed as insufficient by those who favour establishing some kind of global financial regulator with supranational authority, more along the lines of a trade regime. But that latter goal is too ambitious at present, given the strategic place of finance in domestic political economies. Since networked governance is the best achievable goal at this time, G20 initiatives to strengthen it are to be applauded rather than scoffed. Indeed, one hopes the strengthened peer-review mechanism can be mobilized right away to help address the implementation issues mentioned above.

If the G20 leaders do not stay focused on an ambitious agenda, the opportunity for reform will be squandered and the world will stumble once again into yet another major crisis in the coming years.

But more needs to be done to improve the accountability of the FSB and other international standard-setting bodies. To be sure, there has been important recent progress in this area. The FSF was dominated by rich country members, but all G20 countries are now members of the new FSB. The previously narrowly constituted BCBS was also expanded to include all G20 countries this year and other international regulatory bodies have also invited a number of key developing countries as new members.

These efforts to make international regulatory bodies more inclusive are important, but most countries still remain outside, as rule takers. This causes obvious resentment and it is sure to generate a growing political backlash against global standards, especially if the G20 leaders move forward with proposals to develop a toolbox of measures to encourage compliance with international prudential standards among non-cooperative jurisdictions (as they have already done vis-a-vis tax information sharing). The promotion of worldwide compliance is a worthy goal; it will help prevent the kind of regulatory arbitrage that contributed to the current crisis. But it will only be effective and legitimate if it is combined with initiatives to provide all countries with a voice in developing standards.

The FSB and other standard-setting bodies need not become enormous and unwieldy bodies to achieve this goal. More universal country representation could be achieved in a variety of ways, including regional representation or IMF-style constituency systems. Alternatively, the FSB and/or other regulatory bodies could be made accountable to a more universal body such as the International Monetary and Financial Committee of the IMF (or the Global Economic Council of the United Nations that the Stiglitz Commission has recommended).

There is also a risk that including more developing countries in these international bodies will not translate into genuine influence if the technical capacity of the new members does not match that of other officials. To address this issue, technical and research support — preferably via a developing country body such as the G24 — should be provided to help countries develop autonomous and effective voices in these bodies. The need for this kind of voice is strong. Developing countries face some unique issues that could be addressed in international regulatory discussions, but they have not yet received much attention in reform debates. One is the role that capital controls can play in developing countries as counter-cyclical regulatory tools that curtail excessive foreign borrowing in good times and sudden capital outflows during crises. Another is the regulation of commodity futures markets, particularly in the wake of the recent food crisis in developing countries that appeared to be triggered in part by speculative pressures in these markets. A third is the international regulation of capital flight from the poorest countries in regions such as sub-Saharan Africa.

International regulatory bodies need to be accountable not just to more countries, but also to wider societal interests of members. International financial regulatory policy making is dominated by a narrow group of technocrats, often in close conversation with private financial community. The tight nature of this small transnational policy community facilitates international cooperation, but it risks becoming subject to groupthink, captured by private interests and/or unresponsive to the broader public interest. Arguably, the regulatory failures exposed by the crisis can be blamed at least partly on these kinds of dynamics.

To prevent these pathologies, it would be useful to develop mechanisms for wider societal interests to have a voice in international standard setting. In the peer review process which the FSB will coordinate, it would be useful to include at least some reviewers from outside the financial policy area. Transnational groupings of legislators and non-financial officials could also play a role in monitoring the work of international financial regulatory networks, as could an arm's-length body similar to that of the Independent Evaluation Office of the IMF. In addition, non-governmental shadow regulatory committees could be fostered, as could the creation of more access points to international regulatory discussions for citizens' groups. Simpler and more transparent rules should also be encouraged as a means of enabling outsiders to understand and comment on regulatory debates.

Make or Break Time

The G20 leaders placed international regulatory reform at the centre of the agenda for the first two summits for one simple reason: to prevent a repetition of this horrendous crisis. They have made some progress, but the regulatory agenda must remain ambitious at the upcoming Pittsburgh Summit. The following should be priority issues:

- Reinforcing the importance of the implementation of past summit commitments;
- Refining rules for the introduction of macro-prudential regulation;
- Developing policy towards systematically important institutions, markets and products; and,
- Strengthening the accountability of the FSB and other international standard setters to all countries and wider societal interests.

The window of opportunity for significant international regulatory reform may already be closing as the crisis wanes. Failure to revive the political momentum through progress on these issues in Pittsburgh could shut this window further. The result would be depressingly similar to the past: yet another in a long line of failed efforts to comprehensively reform international financial regulation.

Such a failure — given the opportunity presented by the scale and depth of this crisis — would surely discredit the goal of international financial reform and encourage the emergence of a more decentralized and uneven pattern of distinct regional and national regulatory regimes. It would also set the scene for the next, perhaps even larger, international financial crisis in the near future with all its accompanying economic and political costs.

Contrasting Visions of Fiscal Stimulus

Colin I. Bradford, Jr.

Summary Points

- There will be significant pressure for G20 leaders to declare "victory" over the economic crisis at the Pittsburgh Summit. This could be a mistake. Waiting another six months may be wiser.
- There needs to be a highly cautious approach to the issue of when to decide to reach a collective judgment on whether the expansionary fiscal actions taken thus far are sufficient, insufficient or excessive. Jumping on an "exit strategy" too early could endanger the recovery and require a second round of fiscal stimulus.
- The accounting scorecard of fiscal efforts by G20 countries should include both discretionary fiscal actions and expenditures triggered by automatic stabilizers which have been put in place precisely to deal with economic downturns.

In the immediate lead-up to the London Summit, media reports were preoccupied by the different views among Europe, the US and the UK on the degree of discretionary fiscal stimulus being undertaken by G20 countries ahead of the April 2009 meeting. The US and the UK were pressing the Europeans and other G20 countries to develop more discretionary fiscal stimuli, investment programs, tax cuts and other expenditure increases to kick-start aggregate demand as investor, lender and consumer confidence fell dramatically. Fear was now generating a vicious circle downward just as exuberance drove the virtuous circle upward in previous years. The antidote would be a coordinated fiscal policy response by G20 countries at the London Summit. This would reach the level of deliberate coordinated action by major economies achieved only rarely by the G7 and G8 in the past.

Past as Prologue

In the Anglo-American view, what mattered was that the actions themselves be big enough to turn things around, but also that the effect of those visible, significant and coordinated actions on public perceptions and confidence would help turn the global economy around. It was, in effect, an outdated view of summitry, focused too much on what leaders would pledge to do rather than what they were already doing. It was a difference between summitry as performance versus coordination.

The Europeans, on the other hand, with stronger welfare programs than Anglo-Saxon countries, argued that "automatic stabilizers" should count every bit as much as boosts to aggregate demand as discretionary fiscal stimulus actions. And the continental Europeans were right. To the worker, the homemaker and the average tax payer, an unemployment compensation cheque in the mail is the same as a tax cut. Expanded welfare payments for poor children and mothers whose incomes have worsened due to the global downturn are the same as a tax cut or an infrastructure investment program that provides someone in their family a job they did not have before.

So the debate about which type of government spending should count in the scorecard of fiscal effort at the G20 London Summit was divisive and distracting from the main success stories. The realities of what G20 countries were doing on both fronts over time were instead downplayed by interest in what new policies they were pledging to put in place at the Summit itself. The degree to which this false debate overshadowed the central message of cumulative fiscal expansionary measures can be seen in how it was marginalized in the media, as the G20's US$500 billion package for the IMF was played as the headline issue.

And yet, the facts are quite revealing. IMF figures indicate that the 19 countries in the G20 (all but the combined EU seat) provide an overall impact on aggregate demand, including discretionary measures and automatic stabilizers taken together, at an average annual rate of 2.6 percent of 2007 GDP for 2008-2010. This is well above the two percent of GDP fiscal stimulus target identified for the London Summit. In fact, Europe's combined share is actually more than the G20 average, at 2.8 percent of GDP for the three years. The US share was 3.2 percent, only marginally higher than the European average.

The cumulative effect of actions taken together across G20 countries resulted in a total stimulus of US$5 trillion, surpassing the 2 percent target set for the London Summit.

The cumulative effect of these G20 actions, taken together across countries and combining the two types of fiscal expansion, resulted in a total stimulus of US$5 trillion — easily surpassing the 2 percent target set for implementation by March 31, 2009. Paragraph 6 of the London Summit declarations recorded the scale of these cumulative actions but, in part because of the spat between players before the Summit and because of an outdated mode of looking only for new actions, this paragraph and its content were ignored.

This US$5 trillion "concerted" fiscal expansion effort by 19 major countries is unprecedented in scale and scope. It is "historic," in the signifier sense of the term. But it was the untold story of the G20, lost in the false debate about what should count and what should not. In the end, the combined fiscal expansion of the G20 countries will be the main achievement of the London Summit in a historical perspective.

The Next Steps

Looking ahead to the Pittsburgh Summit in late September, what should happen now on the fiscal front?

First, this false debate last spring should be forgotten. The accounting scorecard of fiscal effort by G20 countries for the Pittsburgh Summit should include both discretionary fiscal actions and expenditures triggered by automatic stabilizers put in place precisely to deal with economic downturns. The major economies of the G20 and global economy as a whole seem to be responding to the cumulative impact of G20 fiscal expansionary measures taken together. The whole story must be on the scorecard or the world will get the story wrong again, as it did last spring. The same mistake should not be repeated.

Second, there needs to be a highly cautious approach to the issue of when to decide to reach a collective judgment on whether the expansionary fiscal actions taken thus far are sufficient, insufficient or excessive. It would be enormously damaging to the recovery if a premature conclusion is reached that expansionary fiscal policies will achieve the anticipated turnaround and they are curtailed too soon. Premature contraction could well lead to a "W" curve in recovery, wherein a dip follows the initial rise, requiring another round of fiscal actions. Providing a longer interval for the current measures to work their way through the system would enable a "U," or even a "V," type of recovery path. The Pittsburgh Summit in September could be too early to tell whether the US$5 trillion package is working or not. It seems to be working, but September will be too early to tell. It would make sense to hold judgement until the next G20 summit, anticipated for South Korea in the spring of 2010.

Third, the other danger in this domain would be to prolong the fiscal measures too long or overdo them in terms of both duration and scope, thereby running the risk of generating inflationary pressures down the road. This is a risk that conservatives, especially Republicans in the United States, have been raising throughout 2009. It is certainly a risk that bears watching. Again, timing is critical. Jumping on an "exit strategy" too early could endanger the recovery, and require a second round of fiscal stimulus which would unsettle markets and create a cyclical dynamic in the recovery. In fact, a steady trend is needed. An overly risk-averse approach to inflationary risks in the long run could create further instability and cyclical behaviour in the short run. What the world economy needs is a steady path to recovery without abrupt shifts in policy, turning up the heat one minute and turning it down the next.

Conclusions and Recommendations

Looking ahead to Pittsburgh, given this history of contrasting visions of fiscal stimulus which was actually the driver of the London Summit, the foremost lesson is to avoid repeating the mistake of adopting a partial view of what constitutes fiscal expansionary actions. In this spirit, the G20 should:

- Count both new, deliberate, discretionary measures and embedded, programmatic, automatic stabilizers in the fiscal stimulus scorecard for Pittsburgh. Count everything because everything counts;
- Be careful not to jump to conclusions too soon as to whether fiscal actions taken so far are sufficient, insufficient or excessive. It may be too early to tell by late September. "Wait and see" does not make great headlines, but it may be the best thing to do for the global economy and for the long-run confidence of markets and consumers in global leadership. Determining when to decide is as important as what to decide; and,
- Promote policies that encourage "steady-as-she-goes" activity. The global economy needs predictability over the short, medium and long run. Turning up the heat, then turning down the heat only to have to turn it up again is not the steady, gradual pathway that will bring the economic recovery the world is looking for. The appearance of action for action's sake may satisfy leaders' desire to look decisive, but in economics the right actions generate the results people expect of leaders and ultimately yield the respect and support leaders need to be effective. Economics and politics have to go together for summits to work.

Summits are a narrative through time which creates relationships between leaders and their societies. The trajectory and path of the narrative are more important than the episodes and events of the summits themselves. The success of summits is determined primarily by keeping the story line straight and not letting minor lines become the main story.

In London, the debate about what to count in determining what constitutes enough fiscal expansion wiped out the main story: the scale and scope of the combined collective effort undertaken. Mistake. In the end, the combined action of G20 countries on fiscal expansion worked. Keeping to the main story line and on message are big factors in transforming summits from photo-ops into opportunities to create interactive relationships between leaders and their publics, which ultimately make them effective means of global leadership.

Facilitating Global Lending and Vital Reforms

Bessma Momani

Summary Points

- The SDR-denominated notes are a promising compromise at the moment, and could create added confidence in the idea of an international reserve currency, but this will not quell emerging market economies' deeper desires for added quota and voice reforms.
- The G20 needs to continue encouraging capital-surplus countries to commit more funds to the IMF. China and Saudi Arabia, for example, have remained reluctant to infuse more capital without proportionate increases to their quotas.
- If directed by the G20, the IMF will expedite its general review of quotas in 2011 in the interests of shoring up the financial system.

Pledging in total US$1 trillion dollars to the international financial institutions — from countries that include Japan, the United States, Switzerland, Norway, the European Union and Canada — the G20 London Summit resulted in the largest financial commitment in history to assist the global economy. One half of the total commitment was dedicated to the coffers of the International Monetary Fund (IMF), thereby tripling the Fund's lending capacity. This clearly represented a renewed commitment on the part of those creditors to shore up the financial capacity of the IMF.

With this renewed mandate, the IMF will face the challenge of meeting the needs of countries combatting financial difficulties in these turbulent economic times. The task before the IMF, however, is different now than in previous financial crises of the 1970s, 1980s and 1990s. Today it is the emerging market economies and oil producing states that have the surplus capital to shore up international financial liquidity. Yet, these capital-surplus members are not interested in the IMF, because they view the Fund as an institution that reflects the outdated economic power of the Europeans and Americans.

Nevertheless, the IMF's lending capacity will be enhanced with the infusion of bilateral government loans into the IMF's quasi credit line, the New Arrangements to Borrow (NAB). The IMF claims it will increase its lending capacity further by issuing SDR bonds or notes, by selling parts of its gold reserves and expediting a general increase in its members' quotas through its main account, the General Agreements to Borrow (GAB). With renewed IMF capacity, how can the G20 assist in facilitating the smooth functioning of global lending and what are the implications of the renewed IMF capacity to global economic governance?

Assisting the Smooth Functioning of Global Lending

In a new attempt to shore up IMF finances, the Fund will issue nearly US$150 billion worth of SDR-denominated securities for purchase by member states and their central banks. These tradable, short-term (approximately one year), interest-bearing IMF bonds will be denominated in SDRs (a basket of US dollars, euros, Japanese yen, and pounds sterling), available only at multilateral and development banks and not for sale on secondary or private markets. The commitment to purchase these bonds by China (US$50 billion), Russia, Brazil, India and South Korea (US$10 billion each) indicates great promise that there will be a venue to shore up needed liquidity in the system. For many of these countries, the SDR notes are a means of contributing funds to the IMF, which promises quick exchangeability of notes for SDRs. These emerging market economies have implicitly moved away from putting their money into the NAB because it does not translate into added IMF quota and, hence, decision-making power at the Fund.

The SDR notes are a promising compromise at the moment, but this will not quell emerging market economies' deeper desires for added quota and voice reforms by adding funds to the General Agreements to Borrow facility. More interestingly perhaps, the SDR notes will help countries with large dollar reserves to slowly diversify their holdings without great disruption to the international monetary system. The SDR-denominated notes could, with time, create added confidence in the idea of an international reserve currency denominated in the SDR. While the issue of an SDR reserve currency may not garner consensus at the G20 at present, particularly among industrialized countries, the G20 should agree to study the issue based on the experience of the IMF's SDRs.

With renewed IMF capacity, how can the G20 assist in facilitating the smooth functioning of global lending, and what are the implications of the renewed IMF capacity to global economic governance?

The Fund also plans to initiate the partial sale of its gold holdings to help finance its own operations. The G20 proposed that the Fund consider using a proportion of the gold sales to create a facility of US$6 billion to be used by poor countries on concessional, low-interest and flexible terms. It would be devastating to see the gains made by globalization diminish if poor countries, which have less access to private capital and foreign investment in these dire economic times, descend into greater poverty and, possibly, social and political unrest.

The G20 should continue efforts to ensure the IMF and other international financial institutions continue to offer generous loans to the poorest countries with politically sensitive forms of conditionality. But, the G20 should also commit some of these funds to implement debt relief for heavily indebted poor countries, which are likely to never repay their debts. This debt relief should be considered in the context of encouraging countries to achieve the Millennium Development Goals. More effectively, perhaps, the G20 should discourage its own members from channeling bilateral foreign aid and grants to countries where there are gross human rights violations and continued failures to implement good governance.

The IMF has also proposed another rendition of a quick disbursing loan facility that provides high amounts of lending without conditions; but, the Flexible Credit Line (FCL) is for those members deemed to have favourable policies in the first place. Much like its predecessors, the FCL suffers from the unintended consequence of a shaming effect — where countries worry that signing an IMF insurance policy is a sign of ill-health that could stifle foreign investment. The fact that Mexico has signed an FCL with the IMF is a sign of relief to the Fund; a powerhouse like Mexico has moved beyond the stigma of an agreement with the Fund in the interest of prudent macroeconomic management. If more countries sign FCL agreements, the IMF will have succeeded; if countries shy away from the facility, or if many of the members who need the facility fail to prequalify, the FCL may require some revisions.

While a number of industrialized countries have committed bilateral government loans to the IMF to shore up its lending capacity, the G20 needs to continue encouraging capital-surplus countries, such as China and the oil-producing Gulf states, to similarly commit more funds to the IMF. The reluctance of these capital-surplus countries to invest in the IMF is partly related to their perceived alienation from real IMF decision-making power. While both China and Saudi Arabia hold seats at the IMF Executive Board, they remain reluctant to infuse more capital into the Fund without proportionate increases to their quotas.

The problem herein is in part that quota weights are relative. An increase in one country's quota adjustments requires a decrease in another's — eyes here are mainly on the overrepresented European countries. The other complication is that committed bilateral loans will be placed in the decade-old NAB and have no effect on quota allocation. Simply put, the funds committed to the NAB will not change members' voting strength. Without increases to the relative representation of these capital-surplus members, they will remain uncommitted to shore up the Fund's capacity and resources.

Implications of Renewal of IMF Capacity to Global Economic Governance

Through the G20, powerful members need to address capital-surplus states' concerns and ensure that financial contributions correspond to added political weight at the IMF. This factor points to the overall weakness of the current governance structure at the IMF, which utilizes a weighted quota system that can only lead to a zero-sum conclusion. For one member to gain voice and quota, and hence power and influence at the IMF, another member must give up some of its relative weight. For this reason, the G20 needs to encourage a more flexible governance body that mirrors the changes in the economic and financial system. The proposal to create a Council of Ministers with strategic oversight above the Executive Board is therefore promising; but, the membership of the council needs to flexible enough to accommodate changes in the international financial and economic system.

With G20 support, the IMF will expedite its general review of quotas in 2011 to allow for an overall increase in the Fund's lending resources and the GAB. The implications of redistributing power in the organization will necessarily result in intense negotiations. Adjusting the weighted quota system will yield winners and losers in 2011. In the interest of shoring up financial liquidity, the G20 may have to contend with losing the legitimacy among poorer countries that will necessarily lose out on quota increases. Raising these poorer countries' basic votes in Fund decision making may allay some of their concerns, but improving Fund lending facilities to be more sensitive to debtors' political economy might also improve Fund legitimacy in the long run.

The zero-sum gains of quota reforms will inevitably lead to many disappointments. The time may be ripe to convince the Europeans to agree to lower their representation at the IMF. After all, many European countries, particularly in Eastern Europe, have been knocking on the doors of the IMF for assistance, adding pressure to shore up IMF finances. This can best be achieved through adjustments to the quotas and votes of emerging market members who are ready to contribute funds to the IMF and thereby increase the GAB. The G20 should, at minimum, aim to reform the quota system to better reflect the international distribution of economic power, which will allow emerging market economies to increase their quota shares and correspondingly add lending resources to the IMF's General Agreements to Borrow account.

Kick-Starting IMF Reform

As the IMF grapples with trying to augment its lending capacity, the issue returns to the longstanding one of reforming global economic governance and decision-making power at the IMF. World leaders have an opportunity at the Pittsburgh Summit to advance an agenda of reform.

To set these important tasks in motion, the G20 should:

- Encourage a flexible and more representative governance structure that properly reflects the current distribution of global economic power;
- Continue to ensure the IMF and other international financial institutions offer generous loans to the poorest and most vulnerable countries with politically sensitive forms of conditionality, while implementing debt relief for heavily indebted poor countries; and,
- Agree to study the issue of an SDR-denominated international reserve currency, based on the current experience of the IMF's SDR notes, and support a comprehensive review of the IMF quota system by 2011.

The Challenge to Global Trade in the Financial Crisis

Alan S. Alexandroff

Summary Points

- The G20 has failed to adhere to the Standstill Provision, originally advanced at the Washington Summit, to reduce incentives for protectionist measures.
- While there has not been a rise in protectionism across the board, the surge in national industry bailouts, stimulus packages and subsidies has worrying aspects and even a trend of including foreign commercial discrimination to protect domestic jobs.
- The WTO should work to build acceptance for the "smallest" agreement possible and finally end the Doha Round, before more damage is done to the organizations legitimacy to resolve future conflicts.

The global financial crisis has triggered an unprecedented fall in world output and trade. For 2009, the World Bank has predicted a global economic decline of 2.9 percent, a stark contrast to growth of some 2.1 percent in 2008 and the annual growth rates of nearly 4 percent from 2004 through 2007. The fear of rising trade protection that gripped world leaders led in part to the first G20 Leaders Summit in Washington, DC, in November 2008. While pushing forward on financial regulatory reform, they were quick to commit to an open global economy. In their communiqué, G20 leaders declared it critically important to reject protectionism and avoid turning inward in the face of falling growth and rising unemployment.

The G20 committed to the following: "In this regard, within the next 12 months, we will refrain from raising new barriers to investment or to trade in goods and services, imposing new export restrictions, or implementing WTO inconsistent measures to stimulate exports." And for extra emphasis on the importance of trade to global economic health, they tasked their trade ministers to achieve the following: "Further, we shall strive to reach agreement this year on modalities that leads to the successful conclusion to the WTO's Doha Development Agenda with an ambitious and balanced outcome."

The trade concern has not receded in the months since the inaugural Washington Summit. In the London Summit declaration of April 2009, the leaders renewed their public commitment to what was known, by then, as the "Standstill Provision" and agreed to extend it through 2010. On the question of completion of the Doha Round, the leaders reaffirmed their commitment to reach "an ambitious and balanced conclusion." At the July 2009 G8 L'Aquila Summit, world leaders reaffirmed their commitment to successfully conclude the Doha Round by 2010. They also requested their trade ministers "to explore immediately all possible avenues for direct engagement within the WTO and to meet prior to the Pittsburgh G20 Leaders Summit."

The Threat of Rising Trade Protection

The onset of the global financial crisis saw serious global trade deterioration. After a 27-year boom, predictions for 2009 suggest a contraction of some 9.7 percent in global trade. Even for those countries that achieved spectacular trade growth over previous years, most notably countries like China and India, realized a significant percentage trade decline. Month-to-month changes varied widely.

And for the advanced countries — as measured by the EU or G7 — there was a persistent decline in exports and periodic declines in monthly imports as well. The decline in trade and the explosion of unemployment across the G20 countries as the financial crisis spilled over into the "real economy" raised grave concerns that the domestic response would be to erect trade barriers to protect domestic production and workers. As noted above, the G20 leaders were alert to such a reality, acknowledging the response to the last great crisis, the Great Depression of the 1930s. As the leaders declared at London: "Reinvigorating world trade and investment is essential for restoring global growth. We will not repeat the historic mistakes of protectionism of the previous eras."

Since the Standstill Provision, the G20 countries have implemented at least 41 measures that are almost certainly likely to discriminate against foreign commercial interests.

On January 22, 2009, Pascal Lamy, director general (DG) of the World Trade Organization (WTO), referred to the global trading system as "an insurance policy against protectionism." To enhance the trade system, Lamy declared that the WTO would issue periodic reports on global trends in international trade policy developments as part of the WTO's surveillance mandate. The DG's hope was that members would find these reports useful in facilitating discussions to cope with the crisis. At the London Summit, the G20 urged the WTO and other international bodies "to monitor and report publicly on our adherence to these undertakings on a quarterly basis."

So how determined have the G20 countries been — apart from pronouncements at the G20 summits — in avoiding protectionism? Both the WTO and the World Bank have monitored and published various aspects of trade policy since the Washington Summit. Both have raised concerns about troubling trade policies. However, the WTO only collects information related to possible breaches of the WTO-covered agreements, while it has become evident that many state trading measures have included nationalist and indeed potentially discriminatory measures. To address this gap, a number of leading think tanks — including Centre for Economic Policy Research (CEPR) and CIGI — have come together to initiate an independent global effort to monitor all state measures that might discriminate against foreign commercial interests, identified as imports, exports, foreign investments (including intellectual property) and foreign employees.

Table: Global Trade Alert - Trade Measures

G20 Total	
Measures in the database	89
Measures implemented	53
Measures to be implemented (all countries)	83

By Country	Red	Amber	Green
Argentina	2		
Australia	1		1
Brazil	1		
Canada		9	
China	2	3	
EU	1	1	1
France			1
Germany			1
India	1	2	
Indonesia	6		
Japan	5	1	
Korea	1		
Mexico	2	1	1
Russia	9		
Saudi Arabia	3		
South Africa		1	
United Kingdom	1		
United States	6	19	2
TOTAL	41	37	7

With the assistance of trade experts from across G20 countries, the Global Trade Alert began to collect trade measures that might discriminate against foreign commercial interests and post them on a consolidated website (http://www.globaltradealert.org). The table above summarizes the measures initiated by G20 countries since the Standstill Provision, through to August 1, 2009. The measures are distinguished by their effects on trade partners:

- Red: the measure has been implemented and almost certainly discriminates against foreign commercial interests;
- Amber: the measure has been implemented and may involve discrimination (often these measures have discriminatory aspects and aspects that are either non-discriminatory or even liberalizing). These measures could also have simply been announced or are under consideration and would, if implemented, be discriminatory; and,
- Green: the measure has been announced and involves liberalization on a non-discriminatory basis or the measure has been implemented and involves no further discrimination and is likely to improve transparency.

Thus, since the Standstill Provision, the G20 countries have implemented at least 41 measures that are almost certain to discriminate against foreign commercial interests. Of the measures initiated by G20 countries through August, some 46 percent are almost certainly discriminatory. While there are trade measures that improve trade, the number of discriminatory measures is significant. This record cannot be seen as adherence to a global commitment. Now, while there has not been an across-the-board rise in protectionism — and this is a relief to trade experts — nevertheless, the surge in national industry bailouts, stimulus packages and subsidies include worrying aspects and a trend of foreign commercial discrimination to protect domestic jobs.

Bringing an End to the Doha Round

If G20 leaders have been less than vigilant when it comes to maintenance of the Standstill Provision, what then of their commitment to successfully end the

Doha Round? Here, too, it seems the rhetoric far exceeds the commitment.

After a number of false starts, the negotiation round launched at Doha in late 2001 to provide a cooperative framework for fair market access to developing countries has experienced as many false conclusions. From the outset, much convincing was required of developing countries, especially the poorest in Africa, that trade was good for development and that this Round would bring them substantial benefits. Though the Round was supposed to deal with development issues, in fact it came down to concern with agriculture and non-agricultural manufactured products (NAMA). Originally hoped to reach conclusion by January 2005, the start-stop negotiations have been painfully prolonged.

Doha mobilized a set of new coalitions among Southern countries, most prominently the G20 trade coalition (not to be confused with the current leaders' G20 summit). Operated under various guises, it was led by the "Big Three" (China, India and Brazil) and populated by a number of developing countries. But similar efforts to construct a "new geography," combined with the economic rise of China and India, have led not to a successful conclusion of the Doha Round, but to a grinding stalemate. By blocking consensus — the continued basis for WTO decision making — the Big Three have exerted power, but cannot reach agreement with developed countries.

Following the Washington Summit in November 2008, senior officials in Geneva failed to make progress in the five critical areas identified by WTO DG Lamy: NAMA, tariff cutting, initiatives for specified sectors, the special safeguard mechanism for developing countries to protect against agricultural import surges, and the issue of NAMA preference erosion. With this setback, DG Lamy called off the December 2008 ministerial meeting to mark negotiator progress.

At the London Summit in April 2009, the G20 restated its preference to conclude the Round by 2010. Subsequently, on July 24, 2009, DG Lamy expressed to the Trade Negotiations Committee in Geneva that he anticipated a very busy fall for all negotiation groups concerned with elements of the Doha agenda. He felt:

> … a genuine and strong renewal of political commitment to re-engage in the Doha negotiations and to conclude it in 2010. There were expressions of the need to fill in remaining gaps as soon as possible and of the desire to enhance transparency and understanding of what is on the table. I was encouraged by the determination to avoid theological discussions and instead engage in the common purpose of finding a pragmatic way forward. In sum, a change in atmospherics and a point of arrival.

Yet just a few days later, Rahul Khullar, India's commerce secretary, publicly stated that completion of the Doha Round was out of reach, given public anger over job losses and the lack of economic growth. A successful completion is possible, of course, but the rhetoric of the G20 may pale, perversely it would seem, against the reality of high unemployment and slow growth. It may be that in these circumstances the smallest concurrence among the trading states should call the Doha Round to an end.

Recommendations

While not insurmountable, the challenges presented to global trade by the global economic crisis demand appropriate recognition. Towards the Pittsburgh Summit, the G20 should:

- Publicize the failure of the G20 countries to adhere to the Standstill Provision. In parallel and sustained practice, trade experts should underline the measures where discrimination has been allowed and call for revisions to eliminate such discrimination;
- Accept the "smallest" agreements possible towards a conclusion of the Doha Round, before more damage is done to the legitimacy of the WTO. While not the preferred outcome, the WTO should anticipate that continued effort at a broad agreement will break against the reality of domestic opposition; and,
- Encourage open discussions at the WTO — without concern to negotiate changes immediately — following the end of the Round to examine the sources of discrimination that lie not so much with the issues that concern the current Doha Round, but on matters evident from the current economic crisis: discriminatory procurement, bailouts and subsidies.

Finding a Way Out: Central Banking in Challenging Times

Pierre L. Siklos

Summary Points

- The macro-prudential monitoring role of the central bank should be made more explicit, particularly with enhanced emphasis on systemic risks.
- The present crisis has made clear existing weaknesses in the governance structures of some central banks, identifying a need for formal rules on their independence, ability to implement policy in crisis, and deal with conflicts with their principals.
- At the macro economic level, we have learned that monetary policy, while still effective at the zero interest rate lower bound, does require an entirely different communication and implementation strategy at that level.

Policy makers have turned their attention to formulating rules and regulations that will govern future activities, not only of the financial sector, but of economic policy making more generally. After all, what began as a problem in a particular segment of the US financial sector mushroomed into a global financial crisis, followed by a severe recession in many parts of the world. This put paid to notions that the health of the financial and real sectors of the economy can be separately managed and to the belief that large parts of the world can remain immune from severe shocks originating in a large country, or in a significant sector of the global economy.

The reaction of central banks and governments appears, at least on the surface, to have mitigated the possibility of a cataclysmic failure in the financial system with the resulting repercussions too dreadful to contemplate. Thoughts are now turning to the unwinding of extraordinary measures taken during the crisis.

Somewhat ironically, since central banks in developed countries have come under intense scrutiny since the onset of the crisis, emerging market and other developing economies have been better able to withstand what is likely the largest global economic shock in a generation precisely because, over a decade ago, they began to take seriously the practices of modern central banking. Although this article concerns mainly central banking in developed economies, we should remember that a growing shared belief in some of the core principles of "good" monetary policy, and the development of institutions and mechanisms to help countries carry out the necessary reforms has probably contributed to stemming the spread of the crisis to the emerging economies. Hence, greater efforts at identifying such shared belief in the realm of financial regulation and crisis management should be one of the priorities of policy makers in the G20.

Reacting to the Crisis

In the industrial world at least, one finds a number of common as well as idiosyncratic responses to the crisis. Among the common responses is the global drive to quickly reduce policy rates to record low levels. Although a large number of central banks responded in this fashion, the speed with which interest rates fell, particularly in late 2008, and the timing of interest rate reductions varied considerably across countries. All central banks, including the US Federal Reserve, were not only responding to domestic economic conditions, but were fully aware of what other central banks were contemplating and the pressures they faced.

There should be clear demarcation lines regarding the authority of the central bank versus that of the Treasury, lest the central bankers' maxim of "doing no harm" when it comes to policy interventions be violated.

This reaction did not require a "global" regulator, merely an understanding of what all central banks had already recognized over the years was essential, namely to share information with each other, but also to make publicly available the general economic conditions each were facing at the time. The significant improvements in central bank transparency partly help explain this development. Perhaps less visibly, and arguably less successful, was the desire of policy makers to tackle jointly the issue of systemic risks and the assignment of macro-prudential supervision as between the central bank, existing agencies or potential new agencies. The more difficult question which asks how such agencies would coordinate and/or cooperate internationally has, so far, been left up in the air.

The Current State of Play and Lessons So Far

Despite lofty words expressed in the final communiqué of the London G20 Summit in April 2009 to the effect that the international community would band together to ensure that regulatory and policy frameworks would work harmoniously to ensure financial system stability and economic prosperity, there is a growing realization that "one size does not fit all" when it comes to regulatory reform. Beyond the fact that idiosyncratic responses that are a function of the existing legislative constraints and other institutional restrictions that various central banks operate under, central banks should not be dragged into becoming agencies of industrial policies — history suggests that when a central banker becomes a partner in activist industrial policies, the consequences are typically disastrous. These activities are for this reason not normally in the realm of responsibilities associated with central banking or monetary policy. Ideological constraints also influence the choice of policies. This may determine whether outright bailouts versus other forms of assistance to the private sector are adopted. Indeed, whether the "too big to fail" doctrine that has long preoccupied academics and policy makers can be addressed in a manner that does not unduly impinge on the market's scope for action, and recognizes the desirability of the weak and inefficient to fail while permitting the strong and efficient to prosper under an improved regulatory framework, are also influenced by ideological considerations.

There is the danger that, with the worst apparently behind us, the wrong lessons will be learned. First, in spite of declarations of "never again," crises will never become a thing of the past. Systemic types of crises are more common than realized though, of course, the present one may be particularly severe. Second, policy makers should be careful not to exaggerate their ability to implement a framework to deal with future crises. At a more general level, it is difficult to believe that regulations and enhanced macro-prudential monitoring will outlaw the development and persistence of "global imbalances" though their size might be curtailed. Such macroeconomic imbalances are a regular occurrence and history is full of such imbalances leading to the end of some monetary policy framework.

At the macro economic level, we have learned that monetary policy, while still effective at the zero interest rate lower bound, does require an entirely different communication and implementation strategy at that level. Second, systemic risks in a world where technology progresses at a prodigious rate are greater than we think and can easily threaten financial system stability. Third, we have yet to come up with a workable definition of financial system stability than can permit policy makers to allocate responsibility for its maintenance to the appropriate agencies. And, since monetary policy cannot at all times be asked to shoulder the entire burden of counter-cyclical policies, there should be clear demarcation lines regarding the authority of the central bank versus that of the Treasury, lest the central bankers' maxim of "doing no harm" when it comes to policy interventions be violated. As a result, there is an urgent need to indemnify the central bank against losses when it intervenes in emergency situations, as in recent reforms to the Banking Act in the UK. Perhaps most difficult of all is the need to better understand the consequences of an environment of economic stability, low inflation, and low risk premiums for subsequently greater appetite for risk, the development of asset price bubbles, and the ensuing financial instability.

Finally, the present crisis has made clear existing weaknesses in the governance structures of some central banks. There is a need to revisit some lessons from the past. Governance structures need to be in place to defuse situations in which the central banker, like its cousin the regulator, ends up being captured by those who appoint them. There are plenty of existing models, albeit imperfect, that go a long way toward accomplishing this objective. Nevertheless, a solution must include formal rules about how central banks deal with conflict with their principals and, possibly, limitations on the reappointment of the CEO of a central bank.

Central banks have an opportunity to declare more clearly the circumstances under which current extraordinary policies will be unwound. They also need, in light of criticism of some of their actions affecting events leading up to the crisis, to provide credible means to convince markets and the public that their reaction to it does not contain the seeds of the next crisis. The fact that some prominent economists have welcomed a return to a mildly higher inflation is not helpful nor does it contribute to enhancing the position of central banks. In turn, central banks have turned in a less than stellar performance in convincing the public that low and stable inflation remains the best option. Clearly, the G20 is one forum where the monetary policy makers can more forcefully make their case.

Conclusion and Recommendations

The following recommendations should be considered by policy makers as they contemplate a new policy regime in the wake of the events of 2007-2009. The proposals are not listed in order of importance and should be seen as part of a wider package of reforms.

- Central bank legislation should lay out more explicitly how central banks react in crisis situations, the limits of their responsibilities, and underscore not only the role of government in these situations, but the need for the fiscal authorities to be financially accountable for any extraordinary liquidity/credit measures taken under such circumstances. In addition, the temporary nature of these activities needs to be made clear. Therefore, the exception should not become the rule.

- The macro-prudential monitoring role of the central bank should be made more explicit. This can either be made clear through a minor change in existing central banking legislation or, since central banks typically have a broad mandate, the enhanced emphasis on monitoring systemic risks can be made more explicit in a memorandum of understanding between the central bank and the government.

- Any reform must take account of the fact that whereas any "early warning" type system might rest with the central bank, other agencies of government (for example, deposit insurance agency, financial supervisor(s)) will have an important stake in dealing with future crises. The shared responsibility for acting in concert is one that governments must make clear and for which they must design a regime for accountability (the concern is to prevent a recurrence of the failure of different agencies to act in the common interest, as arguably took place in some G20 countries).

- Central bank legislation must take more seriously how potential conflicts between monetary and fiscal policy are to be resolved and the institutional responses under the circumstances. The reappointment of the governor, if reappointment is to be allowed, must be made a credibly arm's length process. Alternatively, reappointment should not be permitted in some instances to shield against undue political interference when this is likely.

- Policy makers should eschew attempts at regulating an end to global imbalances. These will inevitably reappear from time to time. Instead, greater effort should be made at introducing reforms that permit the authorities to deal with the crises that will almost certainly re-emerge in future. In so doing, the principle of central bank autonomy must be retained and central bankers should be freer to protest and be heard when they see others as threatening economic and financial system stability.

- As noted earlier, even if domestic considerations rule, a better international regime can still emerge. Cooperation at an international level, the development of a core set of principles that transcends purely domestic pressures can also be developed. In particular, the fact that the industrial world is no longer in a position to dictate to the rest of the world the structure of a future policy regime provides an opportunity for smaller economies that have been relatively resilient to play a more decisive role in the shape of the post-crisis world. Just as, for example, in the area of monetary policy and central banking, there is a fairly universal belief in the desirability of low and stable inflation together with acceptance of the need for financial system stability, it is also plainly clear that this can come in a variety of forms suited to a particular economy or region.

Debating Macro-Imbalances and Global Currency

Gregory T. Chin

Summary Points

- Raising the currency issue to the G20 level may be worth the risks, if such talks could generate enough off setting benefits in the form of a new consensus on international currencies and even global macro-imbalances.
- However, for effective discussions on currency revaluation — particularly the Chinese RMB — the G7 would need to back off hard-line, self-defeating positions and seek to build a new consensus.
- As the US and China are now easing their positions on exchange rates, each of the G20 countries would need to take a step back from narrow definitions of national economic interest, striking a balance between national and systemic needs.

While the issue of macro-imbalances is not expected to be on the agenda for the Pittsburgh Summit, many politicians and think tanks have identified it as a core challenge for the global economy. Trade economists caution that imbalances are not going to be changed overnight. So why do officials and analysts keep raising "imbalances," besides to score political points?

The renowned Brazilian economist, André Lara Resende, has noted that there are basically two currents of interpretation of the present crisis. The first emphasizes a deficiency of the regulatory framework that ultimately led to excess leverage in the financial system. The explosion of ingenuity that followed the development of hedge funds and derivatives, and the securitization of credits, transformed the financial system from a relationship-oriented system into a market-transaction-oriented system. It should have been better or more regulated in order to avoid the resulting excesses.

The second current emphasizes the presence of large international macroeconomic imbalances. As Martin Wolf has suggested, the global macro explanations fall into three camps: the first is the "US profligacy" view, which blames the US for excessive government deficits and private consumption; the second is the "money glut" view, which blames lax US monetary policies; and the third is the "savings glut" view, which blames excess savings outside of the US, particularly in Asia and especially in China, for pushing the US towards the policies it followed. These alternative interpretations have very different political and policy implications in terms of fixing the global economy. The first two explanations place more blame on the US. The third sees the US as more of a passive actor, locked-in to excessive spending in order to correct the savings glut outside of its borders. It blames those parts of the world that engage in excessive saving.

Both currents are partially correct, and above all complementary. The macroeconomic imbalance would not have been so deep and persistent without the extraordinary development of financial markets. Indebtedness and leverage would not have reached such extremes without the international macroeconomic imbalance. To accept that both interpretations are complementary leads necessarily to the conclusion that finding a way to reverse the international macroeconomic imbalance is equally important to redesigning the regulatory framework. So far, the G20 process has emphasized redesigning the regulatory framework, while leaving the macro-imbalance issue largely untouched.

Challenges to the Status Quo

Those who focus on imbalances argue that efforts in financial re-regulation must not work against medium-term growth prospects, and that the only way to ensure they do not is to tackle both regulation and imbalances at the same time. For those who emphasize imbalances, the central question today is how to give a new dynamism to the world economy based on factors different from those that led to the imbalances of the last decades. They argue the US needs to move away from its status as a large current account deficit and external debt country, while the large current account surplus countries (such as Germany and China) need to reduce their surpluses. The monetary policies of these latter countries should not be as tight, and fiscal and monetary policies in the US should not be so lax. Observers emphasizing imbalances also ask, besides the aforementioned adjustments, what will be the institutional framework capable of guaranteeing sustainable dynamism to the world economy without resuming and deepening the imbalances of the last decade.

Finding a way to reverse the international macro economic imbalance is equally important to redesigning the regulatory framework. So far, the G20 process emphasized the redesign of the regulatory framework, while leaving the macro-imbalance issue largely untouched.

A number of globally influential economists, including Stephen Roach of Morgan Stanley, and high-profile thinks tank from the Brookings Institution to Chatham House have recommended that imbalances be put at the centre of the G20 agenda. Why has there been hesitancy to do so? The main reason is that the macro-imbalances issue is politically sensitive. The Chinese and other surplus holders state clearly that the criticism of imbalances is criticism of their handling of exchange rate and trade policies. They are aware that adjustments to exchange rates and pressure on China and Asian countries to increase domestic consumption could take away from their trade competitiveness, which has been painstakingly built up over the past few decades. Whether they have done so fairly or unfairly is up for debate, and largely depends on one's reading of the basis of Chinese and Asian trade competitiveness and global economic fairness. These surplus countries do not support the idea that their trade competitiveness has been built on currency manipulation, and suggest that such arguments are further efforts by the traditional monetary powers, who are now major debtors, to once again externalize the costs of adjustment.

Furthermore, the surplus countries argue that what is needed is to ask who should be the evaluator of sustainable debt levels, and the enforcer if such a level is transgressed. The International Monitary Fund (IMF) has only been able to play such a monitoring role over countries that have borrowed from the Fund. Although the IMF commented on (and even criticized) US macro policy, such advice can be, and has been, ignored by the Americans. The BRIC countries have held strongly that it is the developed country group that has put everyone in the current mess. When faced with passing criticism of macro-imbalances, they respond with questions of the global currency situation. In the past six months, Russia, Brazil, China and, to a lesser degree, India, have all questioned the capacity of the US to be the monetary anchor of the global economy. Implicitly, they question the legitimacy of the US to continue to provide the global currency. Even more to the point, they question whether the US deserves to continue holding the privileges and benefits this has role brought to it, including the option of externalizing difficult adjustment costs when it has run up current account deficits, as it did with Germany and Japan in the 1970s and 1980s.

G20 as Price Taker or Decision Maker?

Not surprisingly, the debate has been sidestepped by government leaders so far. Neither imbalances nor currency have been on the G20 agenda heretofore. The only time the issue has been considered at the G20, en passé, was when currency devaluation (that is, promises not to devalue) was discussed. It has also been alluded to in discussions of enhancing the IMF's Special Drawing Rights (SDRs). The BRICs have proposed that consideration be given to currency diversification in international trade, although they have yet to raise it publicly as an issue for the G20 to discuss. They have proposed that alternative global reserve currency options be considered, including using the SDRs as a potential supranational reserve currency. China, Russia, Brazil, France, and to a lesser degree India, all expressed interest in discussing long-term alternatives for global reserve currency at the G8-G5 talks in Italy in July. While this proposal was ultimately resisted by some traditional G8 members, the G5 group of major emerging economies — Brazil, China, India, Mexico and South Africa — discussed the use of their own currencies to settle trade accounts among themselves, at their own gathering the day before their meeting with the G8.

The potential risk in not addressing the imbalances and currency question openly around the G20 table is the prospect that new regulatory and other measures worked out by "the 20" could work against medium- to longer-term growth and systemic management needs. If central tenets of both the Anglo-American and Chinese export-oriented, massive surplus models have been discredited by the crisis, what is coming out the other end? If left unaddressed, the world also runs the risk that China or other BRICs would seek alternative solutions, outside of the existing institutional mix. This would not be a very constructive outcome for the world community, in terms of finding globally coordinated solutions to these problems. It would also likely mean a world heading toward growing currency rivalry and potential destabilization. The US and China are aware of these dangers, even if their top strategists and policy makers are not discussing the matter in public. These issues are being addressed under the new US-China Strategic and Economic Dialogue. For the global community, it would be helpful if these matters were discussed in a more inclusive and transparent manner, as there are serious systemic impact considerations to be taken into account. One consideration, though, is how currency markets would respond to such open discussions of sensitive international exchange rate issues.

Currencies as Vehicles of Power

The crisis has also created an opportunity for Beijing to work with various regional neighbours to further financial, monetary and trade cooperation. Nervous about maintaining its large dollar-denominated holdings, Chinese authorities have started taking gradual and measured steps to "internationalize" usage of the Renminbi. They have established: 1) currency swap agreements worth US$95 billion with Indonesia, South Korea, Hong Kong, Malaysia, Belarus and Argentina; 2) an agreement with Brazil to encourage trade settlement in each other's currencies; 3) plans to buy SDR-denominated bonds; 4) "settlement trials" to allow a small number of export firms in the trade-heavy Shanghai and Guangdong areas to settle their trade in RMB; and 5) a "net settlement system" to increase liquidity and trading volume in the domestic interbank currency market, and for select Hong Kong-based banks to sell RMB-denominated bonds in Hong Kong.

Beijing is aware that it would be no small feat to shift beyond the dollar system, and so far these diversification steps have been rather tentative. However, the longer-term concern of some observers is the prospect of the RMB rising to challenge the pre-eminence of the US dollar. One question for the G20 is how far this group wants China to go on these currency developments, outside of discussing it with the 20. For these discussions to be effective, the G7 would need to back off hard-line and self-defeating positions, and seek to build new consensus. As the "G2" are now doing in their bilateral dialogue to ease their positions on exchange rates and find new consensus on increasing domestic demand stimulus, all G20 countries need to take a step back from narrow definitions of national economic interest, and pay more heed to conceptions of economic statecraft and economic diplomacy that strike a balance between national and systemic needs.

Systemically Important Debate

The currency and macro-imbalance challenges are systemic issues that demand the attention of the truly global powers, as well as "the 20," who together constitute close to 85 percent of the world's GDP. Forward-looking Chinese scholars also see the utility of a combined G2/G20 approach to tackle systemic issues. Huang Ping of the Chinese Academy of Social Sciences, for example, has encouraged China to play a greater role in the G20, to help minimize the impact of the global financial crisis, and called on Beijing to keep an open mind on a broader set of consultations beyond a G2. At the same time, he says China and the US should work together on many bilateral and global programs, from coping with the global financial crisis to developing new energy and carbon emission reduction policies. "It is not in anyone's interest," he said, "for these two countries to endlessly pick on each other." However, China and the US should resist a tendency to believe that, with their size and wealth, a partnership between them (the G2) is all that is needed to decide important world matters. "The so-called G2 is both unrealistic and problematic to fit in with the traditional Chinese value of a harmonious world."

Putting the currency issue on the agenda for Pittsburgh risks inducing some uncomfortable questions about the US dollar system, and it may cause reverberations in currency markets. The risks could be worth taking, however, if such talks could generate enough off-setting benefits, in the form of new consensus on international currencies, and even global macro-imbalances — matters of major systemic importance. Corrections of these two key problems, through combined G20/G2 efforts, would be in keeping with the value that China attaches to a harmonious world and with US interests. Not to mention “the rest.” Failure to address these two related issues, through collective action, carries the risk of gradually hardening positions, and slow descent into geo-economic and currency rivalry.

Long-Term Lessons from the Crisis

John F. Helliwell

Summary Points

- Countries with stronger social and institutional fabrics are less likely to suffer painful consequences from external shocks of any given size.
- National governments and their associated G20 working groups should think more explicitly about the design of policy frameworks that would provide the best institutional and social supports for well-being.
- The G20 can contribute most to global well-being by broadening the notion of "us" used to value the consequences of policies and institutions.

Just as it takes a serious fire to reveal the quality of a fire department, recent financial and economic events have provided a first real test for the G20. The reasoning for establishing the G20 was always forward-looking, aimed to extend a model of high-level consultation and information exchange to enough countries to represent the emerging global economy. If that initial G20 architecture had not already been in place, supported by regular contacts established among G20 finance ministries and central banks, it would not have been possible to so quickly coordinate global responses. In the process, the G20 has provided crucial elements of the international exchanges and joint actions aimed at achieving mutually supportive policy responses, and developing new institutional and regulatory frameworks to improve the resiliency of the international framework.

Strengthening the Social Fabric

Other articles in this report analyze a variety of specific issues. This discussion is instead devoted to the wider long-term importance of the sorts of linkages provided by the G20 and other local and international means of sharing information, advice and assistance. The base for this assessment is more than a decade of study of the links among well-being, social capital and the quality of government. Within businesses, communities and nations, the extent and quality of shared social connections, especially those that foster higher levels of mutual trust, are primary supports for well-being.

Sometimes the total well-being effects of the social context exceed those provided by the levels of income and employment more frequently used to measure national progress. But the social and economic supports for well-being are best seen as complementary rather than competing. However, this positive synergy can only be achieved where policy makers are equally attuned to economic and social aspects of life, and institutions are designed to ensure their compatibility.

Lessons from Natural Disasters

Earlier experiences of natural disasters, ranging from earthquakes to floods, have shown that the quality of the social context is fundamentally important. Where social capital is high, neighbours rush to help one another, and the process of rebuilding starts before the aftershocks have ended or the flood waters gone. Where social capital is low, fingers are pointed, looting starts, trust disappears. Everyone waits for higher powers to intervene and fix things. In that environment, when national or international aid arrives, it is fought over or siphoned off for private gain, and the ruins remain as mute testimony to communal failure.

A natural disaster gives a chance for the connected community to show its mettle, to exercise and extend the ties of mutual support that are such strong determinants of individual, community and national satisfaction with life. By contrast, a similar event where trust, institutions and the social context are weak drives fresh wedges into existing cleavages as scapegoats are sought, trust drops and a fraying social fabric provides new opportunities for exploitation of the helpless.

Studies of the consequences of the 2004 tsunami in Aceh, Indonesia and Sri Lanka illustrate both possibilities. In Aceh, studies show the tsunami sparked wellsprings of fellow feeling sufficiently strong to override the underlying religious and ethnic tensions, producing what has been called a "peace dividend." Remarkably, the positive effects of working together in the face of the natural disaster were great enough to lead to measures of life satisfaction significantly higher than before the tsunami. By contrast, life satisfaction in Sri Lanka was significantly lower after the tsunami, because the peace dividend worked in reverse. So far from leading people to work together in the face of a shared disaster, the tsunami escalated conflict and an even greater loss of well-being.

The G20 is an important form of international social capital, connecting societies as well as specific policies and common approaches.

What can be done to make the Aceh outcome more likely than the Sri Lankan? Here there is very instructive evidence from Japan. Deliberate and successful efforts were undertaken to build social capital sufficient to stem the tide of blame and shame in the wake of the Minamata disease. These efforts eventually succeeded in recreating hope and livelihoods, permitting the community to become a centre for pro-environmental research, a link to forgotten historical roots and a widely watched case study of how good things can flow from bad beginnings.

Are These Lessons Relevant Now?

Can these lessons from natural disasters be applied to analyze the likely consequences of the current financial crisis and recession? Yes, probably. The general element of surprise is evident in both cases, even if precautions were better developed in some places than others. The parallel hypothesis would be that companies, communities and nations with better social capital are likely to suffer less from unpleasant surprises. High social capital firms are less likely to turn immediately to the pink slip as their instinctive response to slumping sales, and are more likely to rely instead on their top-to-bottom shared trust and commitments to develop imaginative responses to the new environment. Amy Lyman of Great Places to Work reports that the firms ranked by their employees as great places to work in 1998 had substantially higher returns over the subsequent 10 years, with the gap between them and average firms growing during the share market meltdown. Similarly, Canadian well-being research by Haifang Huang and myself for the Canadian Institute for Advanced Research estimates that working where trust in management is one-point higher on a ten-point scale has the same effect on life satisfaction as a one-third change in income. Other research has demonstrated that, in such workplaces, employee turnover is lower and productivity higher.

At the community level, recessions might also be expected to take a smaller human toll where social capital is higher. In such communities even unemployment, which generally hits life satisfaction much harder than would be expected just from the associated loss of income, causes less damage to individual and community well-being. The unemployed in well-connected communities are still involved more fully in their communities, and are more likely to have alternative ways to engage their skills for mutual advantage, just as in the earlier earthquake example. If communities with high levels of social capital are also homes to high-trust firms, they are likely to have smaller increases in unemployment in the first place, for any given pattern of external shocks.

Further research will likely show that similar patterns of effects play out among nations. Countries with strong social and institutional contexts may have faced smaller shocks in the first place, if they were less prone to the self-serving behaviour that fuelled the financial crisis. Iceland, with a high level of social capital (at least before go-go international banking hit town), provides an instructive counter example. More essentially, for any given size of initial external shock, those countries with stronger social and institutional fabrics (and these two qualities are inevitably intertwined) are less likely to suffer painful consequences.

By the same token, taking the longer-term perspective required for policies relating to global warming, countries with high levels of social capital have found it easier to design and implement ways of reducing their impacts on the global environment. Such societies have found that doing the right thing for its own sake, and not because they are forced or paid to do so, increases life satisfaction. This has the effect of turning traditional trade-offs on their heads, and exposing a larger number of win-win policy options. Once the underlying psychological realities are more fully understood, and their implications digested, they can as easily support global as purely national interests.

Conclusions

How does all this link to the G20, and the post-crisis sequence of G20 meetings and working groups?

- First, national governments and their associated G20 working groups should pay more explicit attention to the overall well-being of their citizens, and thinking more about the design of policy frameworks that provide the best institutional and social supports for well-being.
- Second, the G20 is an important form of international social capital. Its meetings and working groups are as important for the connections they provide as for the specific policies and common approaches they are more often counted on to deliver.
- Third, just as with local forms of social capital, the G20 can contribute most to global well-being by broadening the notion of "us" used to value the consequences of policies and institutions.

Technology, Systemic Risk and Global Financial Regulation

Jennifer A. Jeffs and Pierre L. Siklos

Summary Points

- Technology allows policy makers to adopt real-time monitoring on a wider scale than heretofore possible.
- Digital data collection and real-time institutional and market surveillance technologies and applications will inevitably become key factors in the future of macro-prudential supervision. These processes will need to be managed, and there will be political implications for the way in which they are managed.
- At Pittsburgh, the G20 should create a group specifically to propel and oversee the development of technology to enhance international supervision and management made up of technical experts, state officials, and IFI representatives.

Communications technology has played an extremely important role, arguably a definitive one, in facilitating the growth and expansion of global finance. Real-time information fuelled markets for complex derivative products while technology allowed exponential increases in volumes and velocities of capital flows, accumulation of debt and risk, and, by extension, holds some responsibility for the financial upheavals that resulted in the current economic crisis.

Central banks and some international financial institutions have highlighted how technology has permitted the development of financial products and, just as important, allowed their complexity to rise exponentially. But there is a need to consider how the emerging needs of macro-prudential regulation meant to address systemic risks can also be met through technical and technological means.

Given the fundamental importance of communications technology to the overall operation of the international financial system, and the clear need for new international financial regulatory processes, there should be greater public discussion of the role that technology can play to facilitate these processes and make them both more efficient and politically acceptable.

Technology and Macro-Prudential Oversight

The pressing need for cooperative regulation, information sharing and, in general, networked solutions to deal with the overextension of financial markets is likely to spur important and unprecedented creation, advancement and adaptation of collaborative digital networking technologies. Digital data collection and real-time institutional and market surveillance technologies and applications will inevitably become key factors in the future of macro-prudential supervision. These processes will need to be managed, which will have political implications.

Technology allows policy makers to adopt real-time monitoring on a wider scale than heretofore possible. To date, real-time monitoring has often been confined to financial markets themselves, while the consequences of high-frequency movements in financial markets for the economy as a whole have not generally been explicitly addressed. Central bankers were always aware of the potential conflict between their desire to ensure price stability and sustainable economic growth, and developments in financial markets that threatened the stability of the system. But as recent events have shown, the tools that would allow policy makers to remain on a path between the two shoals of myopic behaviour and tunnel vision has yet to be found.

To this point, the G20 has not advocated for technological innovation, but there is an opportunity to consider how the emerging needs of macroprudential regulation meant to address systemic risks can also be met through technical and technological means.

Meanwhile, policy assessments at the macroeconomic level were dangerously dependent on whether they were based on the data actually available at the time decisions were made, or on the final published figures issued with significant time lags, and frequently revised long after policy announcements were made. Convincing the broader financial industry of the need to collect and make the available data and models public in real-time has been a difficult task, although there are a few success stories that can serve as models for domestic and international institutions.

The current environment, as well as available technology, gives policy makers a unique opportunity to revisit data collection, analysis and dissemination mechanisms, and improve the quality of decision making. Indeed, numerous multilateral organizations and institutions hovered over this type of activity, before the current financial and economic upheaval. The International Monetary Fund (IMF), the World Bank, the Bank for International Settlements (BIS) and the Financial Stability Forum/Board (FSF/FSB) have all played specific roles in the progress of modern international financial life. The IMF, for example, introduced its Special Data Dissemination Standards (SDDS) a few years ago. Originally intended as a vehicle to ensure comparability of a wide variety of macroeconomic, financial and trade data across member countries, it seems to have largely gone unnoticed. Clearly, given available technology, such efforts should receive higher priority in efforts at global reform than has been the case to date.

More recently, several new boards and councils have come into existence, prompting an important question: how will financial monitoring, support and regulation by all the different bodies function both separately and together? How, for example, will the FSB manage to work closely and simultaneously with various and diverse regulatory and monitoring bodies such as the IMF, national regulatory agencies and regional organizations like the European Systemic Risk Council?

The "Council" approach, also evoked in the context of financial regulatory reform in the United States, would allow various regulatory institutions to concentrate on their respective roles, while also enabling crucial monitoring of financial systems and advisory capacities within and across borders. Such an approach to global financial regulation seems to require fairly dramatic technological developments — as dramatic, if not more so, than those that allowed international financial markets to develop into their current state.

Technology, accompanied by mathematical and modeling innovation, can help process the necessary financial technical data, and provide the necessary bridge for real-time cooperation across many people and many organizations in different time zones and with disparate institutional schedules. It provides an alternative to uniformity and its tremendous biases — allowing timely and efficient compilation and correlation of large quantities of data from a wide variety of monitoring instruments and organizations. Much of this data will be highly specific, requiring the analysis of experts in each area, and the need to share this information will produce new and sophisticated adaptations or applications of what have been developed to date as social networking technologies. These technologies will develop along a macro-prudential oversight tangent.

What this means is that a "one size fits all" mentality is not essential for effective macro-prudential regulation in a post-crisis world. Individual countries will be able to note and take account of idiosyncratic characteristics of domestic policy making. As well, for crisis management and prevention, the literature and personal anecdotes acknowledge that face-to-face meetings, and the collegiality and personal relationships they engender, are important. However, as technology develops to allow these encounters to take place in a virtual space, they can occur both more frequently, and be informed by real-time, or at least very close to real-time, data collection, sharing and analyses.

The Development of a "Financial Skin"

The emergence of the G20 is in part a reaction to excessive movement towards "level" playing fields that are not universally level. Thus, it is not only feasible, but also politically important, that the data analysis involved with macro-prudential oversight as it unfolds in a G20-world takes into account and reflects distinctive national historical traits or structures.

Despite some moves toward harmonization, nationally distinctive analyses have grown out of particular circumstances and cultures that will need to be "translated" into international regulatory language in order to provide systemic early warnings for regulators to offset the build-up of systemic risks.

How could this be done? One could take a cue from developments designed to address another global public good issue of enormous complexity, namely climate change. In a powerful example of a private-public partnership created to monitor a public good, Cisco, a large US communications technology company, entered into a commitment in March 2009 with NASA to develop a technology it describes as a "Planetary Skin." This digital platform will create a network for receiving, capturing and tracking worldwide environmental data from satellite and other sources. Both the International Panel on Climate Change and the UN Framework Convention on Climate Change support the project, which includes "sensor networks" for collecting data; decision-making support tools for management of resources, risks and environmental markets; and something that has been labelled a "commonspace" layer to facilitate public and private feedback to decision makers in the field of environmental science.

This partnership will help achieve one of the three basic requirements for mitigating and adapting to climate change outlined by public and private sector leaders at the World Economic Forum earlier this year. This was the creation of "a globally trusted mechanism for measurement, reporting, and verification (MRV)," referring to "planetary skin," an intelligent technology mechanism.

Similarly, the development of a "financial skin" that incorporates the data collected by financial regulatory agencies and monitoring programs with mathematical assessments of systemic financial risk for a technical platform or "skin" seems like a highly likely, if not inevitable, development in international financial regulation. Again, the programming of such technology should be done in a way that does not privilege certain types of financial systems over others, but instead goes beyond historically and culturally determined financial structures and financial industry institutional designs. This system should accurately and fairly assess the accumulation of risk and accompanying build-up of systemic threats in individual national financial systems.

Thus, the technology itself cannot be imposed, but needs to be developed collaboratively. Just as policy makers need to accept that various forms of democracy and capitalism can co-exist, variations of national financial structures and traditions will need to be accommodated and factored into technical processes of data collection and analysis.

Reducing Obstacles to Information Sharing

Previous efforts at coordination have often ended up with the most economically powerful nations imposing their policies — inadequatly, as it turned out — on others. A more collegial approach is undoubtedly going to be more successful than the last one. Technology has the potential of delivering on this collegial approach, and therefore its political and economic benefits. In this framework, monitoring can remain a domestic responsibility because technology should enable even smaller countries to perform the tasks of providing a "second opinion" that is likely essential to build trust and credibility in the new regime.

Data infrastructure costs for the storage and dissemination of data decline very quickly after they are introduced. There is, however, one important constraint that cannot be overcome through technology alone: human capital is not evenly distributed across nations. As a result, some forms of cooperation will be essential. It is here where the role of international institutions becomes crucial. Unless these institutions are capable of delivering needed trust and credibility to policy makers, national governments cannot be confident of reducing the likelihood of another global financial crisis, with or without the application of new technologies.

What is missing, therefore, from the G20 Working Group 1 recommendations, and would work to tie many of them together in a coherent manner, is a G20 group specifically assembled to propel and oversee the development of technology that could dramatically enhance international supervision and management of various financial regulatory areas. Data collection, analysis and monitoring conducted at the domestic level would be fed into a global technology platform. While the platform itself would be built by those with the appropriate technical expertise, the process would be managed by a G20 group representative of the various national financial structures, cultures and regulatory mechanisms in the systemically important countries.

Although progress has been made in the mitigation of crisis-inducing risky behaviour, many financial market observers are far from confident that all aspects of systemic risk are being effectively contained. Systemic risk comes in several categories: operational risk, political risk, credit risk and liquidity risk. Credit and liquidity risk seem more amenable to the adaptation of collaborative social networking/tracking technology than either political or operational risk, which can both involve relatively unpredictable factors. However, liquidity risk is always a partner of each of the other three categories of risk.

Protection against liquidity risk therefore essentially protects against all risk categories, with liquidity risk monitoring naturally flowing from credit risk surveillance. Thus, technology is an element that should be put at the centre of discussions and reforms to reduce global systemic risk.

Summary of Recommendations

- The G20 needs to pay attention to the role that communications technology can play in financial regulatory processes to reduce or eliminate systemic risk. The creation of a G20 group specifically assembled to propel and oversee the development of technology to enhance international supervision and management — made up of technical experts, state officials and IFI representatives — would be a good start.
- Data collection, analysis and monitoring would be conducted nationally, and fed into a global "skin" or digital platform. While the platform itself would be built by those with appropriate technical expertise, the process would be managed by this working group, which would be representative of the various national financial structures, cultures and regulatory mechanisms in systemically important countries.
- As this working group would oversee the development of digital networking technologies, it will be important for the group to understand and work to ensure that distinctive features of national financial systems remain intact, while neutralizing differences in national structures and practices.
- This group should ensure the programming and design of the technology that collects and analyzes financial data does not privilege certain types or designs of financial or institutional structures. A minimum set of flexible but rigorous technical standards that serve as an international benchmark should be developed.

Complex Systems and Global Problems

Thomas Homer-Dixon

Summary Points

- The global economic system's fundamental complexity is unlikely to diminish. More economic crises exhibiting the same features are likely in the future, in the absence of radically different institutional designs and policies.
- Policy makers should recognize that while intractable uncertainty and long time lags may accentuate the political challenge of action on complex global problems, they are not an excuse for inaction.
- Drawing lessons from the recent economic crisis, a major research program should be undertaken to better understand the implications of complex system behaviour for public policy and governance.

Many analysts and commentators have interpreted the recent economic crisis as a decidedly anomalous event. They see it as the economic equivalent of the thousand-year storm — the result of an unhappy but exceedingly rare conjunction of poor regulations, individual venality and bad luck.

This view is incomplete. The economic crisis has actually opened a window on our future. True, the particular conjunction of events in this case was rare. But the crisis is also an example of a more general and increasingly frequent phenomenon: a sudden shift in behaviour of a highly complex system critical to human well-being under extreme and steadily rising stress.

Certain key features of the crisis can ultimately be traced to the global economic system's fundamental complexity. Because this complexity is unlikely to diminish, more economic crises exhibiting the same features are likely in the future, in the absence of radically different institutional designs and policies. Also, because many of humankind's most intractable global challenges — including climate change, energy scarcity and pandemic disease — arise from (often intimately connected) natural and social systems that are similarly complex, important lessons of this economic crisis apply to these other challenges too.

For the purposes of the analysis here, the economic crisis's key features are:

- Advance warning from a few experts of the rising dangers of systemic crisis that engendered little or no policy response;
- Origins in the conjunction of several long-term trends that ultimately produced a sharp and sudden shift in system behaviour from stability to turbulence;
- Rapid worsening because of self-reinforcing feedbacks amplified through tightly coupled networks;
- Extreme unpredictability during its worst phases; and,
- Inability of policy makers to control system behaviour with any precision.

The Role of Complexity

The above features are partly a result of the rising complexity of our modern economic systems. Complex systems, whether natural systems like the global climate or social systems like the global economy, generally exhibit what specialists call "nonlinear" behaviour, which is characterized by a disproportionate relationship between cause and effect. In a nonlinear system, small perturbations sometimes cause big effects, while other times big perturbations have little or no effect at all. Nonlinear behaviour has a range of sources, most importantly the presence within systems of self-reinforcing and self-cancelling feedback loops and of multiplicative or "synergistic" interaction among causes.

The current economic crisis is an example of a more general and increasingly frequent phenomenon: a sudden shift in behaviour of a highly complex system critical to human well-being that is under extreme and steadily rising stress.

In turn, nonlinear behaviour leads to three other characteristics of complex systems: intractable uncertainty, intermittently long time lags between perturbation and response, and the potential to "flip" abruptly from one state to another. These characteristics make system behaviour notoriously difficult to control. Uncertainty weakens policy makers' ability to predict this behaviour and to calibrate the size and scope of proposed interventions. Time lags make it hard to correct suddenly undesirable behaviour, and impede learning about the efficacy of policy interventions to change that behaviour. Abrupt flips demand wholesale reorientations of policy and often preclude returning the system to its previous state.

From the perspective of national and global governance, the combination of high uncertainty and long time lags is particularly pernicious: together, in the absence of a crisis, these characteristics of complex systems give policy makers and publics enormous scope to ignore advance warnings and procrastinate in implementing effective policy responses.

In the face of complex challenges exhibiting uncertainty, lags and potential for flips, conventional "management" policy responses — responses that are conservative, incrementalist, conflict minimizing and grounded in the assumption that social and natural systems operate much like simple machines — are almost always ineffective. In a world of complex systems, planning based on estimates of most likely outcomes can, in fact, be profoundly reckless.

Unfortunately, researchers and policy makers have not developed alternative strategies and institutional designs appropriate for the now radically complex world. This lacuna needs to be addressed immediately.

Complexity and the Economic Crisis

In recent decades, financial crises, especially those that involve both a sharp devaluation of a country's currency and the loss of most of its banking capital, have become more frequent and arguably more severe. But if anything, policy makers have exhibited progressively less ability to predict these crises' advents or their courses as they unfold.

In advance of the most recent crisis, uncertainty was deep and pervasive. While some analysts expressed concern about certain long-term trends — including rising household and corporate debt, increasing vulnerability of the US sub-prime mortgage market, and the progressive attenuation of estimated risk through securitization and derivatives like credit-default swaps — only a few observers (such as Nouriel Roubini) anticipated anything like what eventually occurred. And during the crisis' first eighteen months, from mid-2007 until the end of 2008, policy makers and their economic advisors were wrong far more often than they were right about the likely direction of events, usually vastly underestimating the crisis' future severity.

The financial system also repeatedly flipped from one state to another. The long-term trends combined synergistically to create widespread and largely unrecognized systemic weaknesses. A proximate cause — some research points to soaring energy prices — pushed the US economy across a threshold into recession. Then, a succession of sharp shifts rapidly deepened the crisis. The bankruptcy of Lehman Brothers in September 2008 was an especially critical inflection point: credit markets around the world almost immediately seized while equity markets began a plunge that lasted through the fall. Policy makers and central banks tried to respond by forcing down interest rates, buying near worthless securities from banks and pumping huge quantities of liquidity into financial markets; but, the global economy's lags worked against them. It had developed enormous systemic inertia; a stunning worldwide contraction of investment and consumption and a surge in unemployment overwhelmed responses.

The policy challenges that such crises pose, already diabolically difficult to manage, are made harder by the constant metamorphosis of economic systems and policy landscapes. For instance, self-reinforcing feedbacks, like a fear-sell cycle or a deflationary spiral amplified through tightly coupled economic networks, might start to drive the economic system, crippling standard interventions. Long-tested relationships, between money supply and inflation, can abruptly become invalid. And as understandings of the nature of the crisis shift, the route to "stability and growth" has to be re-estimated repeatedly. One of the most striking features of the recent economic crisis was the "seat-of-the-pants" character of responses through the fall of 2008. Policy makers tried one thing, then another and another — hoping that something, anything, would work.

Coping in a World of Complex Challenges

Other global challenges arise from systems that exhibit the same characteristics of uncertainty, lags and potential for flips. These characteristics are, for instance, inescapable features of the climate system.

Uncertainty arises from our incomplete knowledge of climate feedbacks, especially of self-reinforcing positive feedbacks in the global carbon cycle. For instance, we know that warming will melt Arctic permafrost, which, when it rots and releases carbon, causes more warming — but how bad will this cycle be? How much of the extra carbon will be absorbed by plants that grow faster in a carbon-rich atmosphere?

Lags arise from inertia in the climate system — due to, for instance, the oceans' absorption of heat — that slows the climate's response to carbon emissions. They also arise from the slow turnover of our carbon-emitting energy infrastructure.

Flips appear in the paleoclimatological record (ice core, sedimentary and coral data, for example), which shows occasional sharp discontinuities in ancient climate regimes. Climate scientists now vigorously debate whether human emissions of carbon could soon push the planet's climate over such a threshold. Some argue that the recent dramatic decline in the total area of Arctic sea ice indicates that a wholesale reconfiguration of energy circulation patterns in the Arctic basin may be underway.

As with the economic crisis, uncertainty and lags combine to weaken policy responses to climate change. Publics and politicians ask: why should we pay substantial costs now to avoid an uncertain threat far in the future? Special interests groups and firms that benefit from the status quo — hydrocarbon energy producers, car companies, heavy manufacturing unions and the like — exploit this hesitation by emphasizing the degree of uncertainty in climate science, the temporal distance of any climate costs, and the magnitude and temporal nearness of mitigation costs.

These arguments implicitly assume that humankind can adopt remedial measures if and when the costs of climate change become substantial. But like all complex systems, including the global economy, Earth's climate exhibits "hysteresis" — that is, the system's state at any particular time depends on the path it followed to get to that state (often referred to as path dependency) and movement along that path is not trivially reversible. A return to a previous climate state, especially if the climate has passed a critical inflection point, may be impossible. If it is possible, the climate system will have to return via a path entirely different from the one it followed previously. Put simply, once we find out definitively that we have pushed the climate too far, it will likely be extraordinarily hard to go back to anything like the current climate. The clock cannot simply be reversed.

The Logic of Precaution

In situations where the consequences of a mistaken judgment are potentially catastrophic and irreversible, the logic of Pascal's wager should prevail. In the case of climate change, should policy makers bet that such change is not going to hurt the world badly and use resources to solve other problems? If we are right with our bet, we save some money in the near term; but if we are wrong, the consequence for future generations could be catastrophic. Or do we bet that climate change could indeed hurt the world badly in the future and invest to prevent that outcome? If we are right, our children avoid possible catastrophe; but, if we are wrong, we lose some money in the near term.

Such logic might not always guide our responses to complex global challenges. Even if the consequences of a mistaken judgment are irreversible, policy makers might decide they are unlikely to be catastrophic. But when dealing with systems exhibiting intractable uncertainty, long time lags, and potential for abrupt flips between radically different states, a normative principle of prudence or precaution should generally guide public policy. At the moment, alas, prudence is notably lacking in human affairs.

Recognizing Complexity

The recent economic crisis was an instance of a general type of problem that will become more common in an increasingly complex world. In consequence:

- A major research program should be undertaken to better understand the implications of complex system behaviour for public policy and governance, perhaps using the recent economic crisis as a source of lessons. Examples of key research questions are:
    - How should public policy decisions be made in circumstances where intractable uncertainty (as distinct from risk) shrouds future outcomes yet a wrong decision could produce catastrophic costs? Are there alternatives to conventional cost-benefit analysis?
    - What criteria should govern the design of institutions for democratic decision making about interactions with systems that have multi-decade or century-long time lags between perturbation and response?
    - Do the ecological, biological and physical sciences provide clues as to how policy makers might be forewarned of an impending sharp nonlinearity in a key global system's behaviour?
- Policy makers should recognize that while intractable uncertainty and long time lags may accentuate the political challenge of action on complex global problems, they are not an excuse for inaction.
- Policy makers should also recognize that in systems with the potential to flip their behaviour, past and current systemic trends are not good indicators of future system states.
- In circumstances where uncertainty and lags shroud future outcomes yet a wrong decision could produce catastrophic and irreversible costs, policy makers should generally adopt a precautionary or prudential approach to system governance.

ANNEX I: Overview of Substantial Commitments from Washington, London and L'Aquila

Prepared by Christian Ruiz, CIGI-Hertie School Exchange Student

A. Strengthening the International Financial Institutions

i. Monetary Pledges

Deliberations in the G20 summits and working groups have underlined the importance and application of counter-cyclical measures to boost demand on a global level. At London, this materialized in the pledge of more resources for the International Monetary Fund (IMF), the World Bank, the Financial Stability Board (FSB) and the Multilateral Development Banks (MDBs) (see Box 1). Both summit communiqués stressed bolstering the access to funds — particularly by emerging and developing nations — in order to "resume the private capital flows which are critical for sustainable growth and development."

At the London Summit, greater emphasis was placed on conducting "economic policies cooperatively and responsibly with regard to the impact on other countries," with pledges to refrain from currency devaluations and to promote a stable international monetary system.

ii. Pledges to Modernize International Financial Governance

The reinforcement of international cooperation and the reform of the international financial institutions (IFIs) were accorded high priority at both G20 summits. First of all, members agreed that the resources of institutions like the IMF, the World Bank and MDBs should be reviewed and increased where necessary. Further, the leaders underscored the need to reform decision-making structures in the Bretton Woods Institutions, to "adequately reflect changing economic weights in the world economy" and to increase their institutional legitimacy and effectiveness. Both summit communiqués explicitly mention that emerging and developing nations "should have greater voice and representation in these institutions."

In this spirit, the IMF board of governors should have more strategic direction and more accountability; it was pledged that the heads of all IFIs "should be appointed through an open, transparent and merit-based selection process." The G20 process has revealed the critical functions of the IMF:

- At Washington, members pledged to enhance the role of the IMF in global economic governance, and urged an internal review of its instruments and facilities.
- At London, the IMF was charged to use its analytical capabilities to assess both current actions taken as well as the global actions required from national governments, in particular, to resume and raise global growth to over 2 percent by the end of 2010.

Finally, it was agreed upon that the principles for cross-border crisis management, developed by the former Financial Stability Forum, should be immediately implemented.

Box 1: Monetary Pledges at the G20 London Summit 2009

- Resources available to the IMF were raised by over US$250 billion.
- Incorporating a more flexible arrangement to borrow from the IMF, increased by up to US$500 billion (including existing funds).
- Additional lending of at least US$100 billion by the MDBs, raising this amount to a total of around US$300 billion over the next three years.
- The sale of IMF gold worth US$6 billion.
- Doubling of the IMF's concessional lending capacity for low-income countries and doubling of access limits.
- US$100 billion of the US$250 billion that are injected into the SDR go directly to emerging market and developing countries.
- A 200 percent general capital increase at the Asian Development Bank.
- Voluntary contributions between US$3-4 billion for the World Bank's IFC's Global Trade Liquidity Pool — other voluntary contributions to the World Bank Vulnerability Framework.
- Low-income countries with sustainable debt positions and sound policies should be given temporary access to non-concessional World Bank loans to compensate for the loss of access to capital markets.
- US$250 billion over the following two years were promised to support trade finance through export credit, investment agencies and through MDBs.

B. Reform of the Financial Sector

i. *G20 Commitments*

a) *Global Financial Sector or National Financial Markets?*

A comparison of the vision of both summits is important concerning their most important pledge: the regulation of the financial sector. At Washington, the leaders urged stabilization of the financial system through "strengthen[ing] financial markets and regulatory regimes" at national levels. While at London, the basic understanding of the problem shifted to a stronger but also more "globally consistent… framework for the future financial sector" at a global level. This difference in wording exposes the problem of authority and responsibility in financial regulation, between the national and global. Clarity is needed here, as the understandings of the underlying problems will affect the types of solutions brought forward.

b) *Transparency and Accountability*

Both G20 summit communiqués called for "strengthening transparency and accountability" in the financial sector. This should be achieved by "enhancing required disclosure on complex financial products and ensuring complete and accurate disclosure by firms of their financial conditions."

c) Sound Regulation

Financial regulation should be enhanced by ensuring "that all financial markets, products and participants are regulated or subject to oversight." This regulation should be effective, efficient, encourage trade in financial products and services, and should not stifle innovation. At London, the G20 leaders committed to promote the standardization of credit derivatives — in particular, they agreed on the "establishment of central clearing counterparties subject to effective regulation."

A further important element is the explicit oversight over credit rating agencies, and ensuring that they meet the highest international standards. At London it was agreed upon that credit rating agencies, whose ratings are used for regulatory purposes, should "be subject to a regulatory oversight regime that includes registration."

Members at the London Summit added that regulators should possess the power to conclude stress-tests on financial institutions and therefore be able to predict systemic risks better.

Every G20 member, including those who were reluctant in the past, will also have to undertake a so-called Financial Sector Assessment Program (FSAP) Report to review and report on the national regulatory systems and ensure that they are "compatible with a modern and increasingly globalized financial system."

d) Promotion of Integrity

At Washington, the promotion of integrity included the idea on the one hand of bolstering investor and consumer protection. On the other hand, it included the commitment to take steps to prevent fraudulent and illegal abuses as well as illicit activities like tax-evasion by so-called tax havens (by promoting information sharing regarding banking secrecy and tax transparency).

At London, the last point was stressed much further, declaring that "the era of banking secrecy is over." The leaders agreed on a commitment to stand ready for sanctions against uncooperative jurisdictions — for this purpose a "toolbox" with possible measures was enumerated. In this respect, the Organisation for Economic Cooperation and Development (OECD) published, in parallel with the London Summit, a "grey list" of countries that do not fully comply with international standards against tax evasion.

Executive pay and compensation in financial institutions was also scrutinized at London, where members advanced the agreement on principles, as elaborated by the former FSF. This includes that firms have to "publicly disclose clear, comprehensive, and timely information about compensation" and that bonuses should more properly reflect risk.

e) Reduction of Systemic Risks

The G20 members committed in both summits that "financial institutions should provide enhanced risk disclosure in their reporting and disclose all losses on an ongoing basis" thus showing an accurate, complete and timely picture of the firm's activities. At London, for the first time, it was agreed upon that "hedge funds or their managers will be registered and will be required to disclose appropriate information on an ongoing basis to supervisors," including on their leverage, which is necessary to predict systemic risks.

In a similar vein, systemic risk emerging from "over-the-counter" derivatives will be reduced. Last but not least, supervisors should collaborate to establish supervisory colleges for all major cross-border financial institutions. At London, a deadline of June 2009 was set to complete these measures.

ii. G20 Calls on Other Institutions

a) Enhanced Cooperation between IFIs

The declarations emerging from the Washington and London summits stressed that cooperation among the IFIs on crisis prevention, management and resolution must be strengthened. The text of the first summit communiqué advanced that the IMF, in collaboration with the former FSF and other bodies, should be able to "better identify vulnerabilities, anticipate potential stresses, and act swiftly to play a key role in crisis response." This materialized at London in the commitment to create an early warning system for macroeconomic and financial risks between the FSB (with its focus on standard setting) and the IMF (with its focus on surveillance).

b) Expanded Mandate for New FSB

One of the most decisive achievements of the two summits was the expansion of the former FSF's mandate. At London it was decided that membership must be enlarged (particularly to include emerging economies), the institution shall be renamed the Financial Stability Board and will have a significantly strengthened mandate, including:

- Assess vulnerabilities in the financial system.
- Promote coordination and information exchange among authorities responsible for financial stability (including issues like hedge funds, in order to ensure that effective oversight is maintained where a fund is located in a different jurisdiction than the manager).
- Advise on market developments and their implications for regulatory policy.
- Implement joint strategic reviews of the policy work of the international standard-setting bodies to ensure that their work is coordinated.
- Support contingency planning for cross-border crisis management.
- Collaborate with the IMF to conduct early warning exercises.

c) Valuation of Securities

The global accounting standards bodies should work to enhance guidance for valuation of securities. Weaknesses in accounting and disclosure standards should be addressed by accounting standard setters and a single, high-quality global standard should be the objective. "The governance of the international accounting standard body should be enhanced to promote financial stability, including by undertaking a review of its membership to ensure transparency, accountability and an appropriate relationship [to other relevant authorities]." These commitments were similarly reflected in both G20 summits.

d) Reviewing Basel II

The Basel Committee on Banking Supervision (BCBS) should review minimum levels of capital while also proposing ways to improve incentives for risk management of securitization. At London, leaders called for a report on these activities in 2010.

At Washington, it was agreed that procedures should be implemented to ensure that financial firms implement policies with better liquidity risk management and supervision of their liquidity.

This was also reflected at London, where it was underlined that excessive leverage must be prevented and buffers of resources could be established in a countercyclical manner.

Furthermore, it was elaborated that "risk-based capital requirements should be supplemented with a simple, transparent, non-risk based measure that is internationally comparable [and] properly takes into account off-balance sheet exposures."

e) Promotion of Integrity

Concerning tax evasion in particular, the G8 L'Aquila Summit in July 2009 called upon the OECD Global Forum on Transparency and Exchange of Information to implement a peer-review process to assess the implementation of international standards by all jurisdictions. As an intergovernmental organization, implementation of this initiative would require the approval of all OECD members, including Switzerland and Luxemburg.

C. Open Global Economy, Completion of Doha Round

i. G20 Commitments

One of the most substantive (and newsworthy) commitments made by the G20 at Washington was "to refrain from raising new barriers to investment or to trade" for one year. Known as the "Standstill Provision," this pledge was extended at London to the end of 2010. In addition, there was also a commitment against financial protectionism, particularly measures that constrain worldwide capital flows, especially to developing nations, and to take whatever steps possible to promote and facilitate trade and investment.

Concerning the Doha Round of negotiations through the World Trade Organization (WTO), members declared at Washington in November 2008 to strive for agreement on modalities that would lead to a conclusion of the Round and to make positive contributions necessary to achieve such an outcome. At London, this commitment was reaffirmed and further stressed that it is necessary to renew the focus and to raise political attention. And finally at L'Aquila, a new deadline was set for the conclusion of the Round by the end of 2010.

ii. G20 Calls on Other Institutions

At London there was a call on the WTO, together with other international bodies, to monitor and report publicly on trade-related issues on a quarterly basis. This is combined with a call on regulators to make use of available flexibility in capital requirements for trade finance.

D. Other Issues

i. G20 Commitments

While the G20 has remained well focused on the core economic agenda, it has made declarations on other pressing global issues. At Washington, the leaders "remained committed to" the following topics: energy security, climate change, food security, rule of law and the "fight against terrorism, poverty and disease." At London, greater emphasis was placed on the mitigation of the social impact of the global financial crisis and to minimize effects on the most vulnerable populations. To this

Box 2: Deadlines Decided at the G20 London Summit

- The national supervisors should implement the principles developed by the former FSF on pay and compensation by the 2009 remuneration round.
- The IMF and FSB should together launch an early warning exercise at the 2009 spring meetings.
- The FSB was called on to work with the BIS and international standard setters to develop macro-prudential tools and provide a report by autumn 2009.
- The financial industry should develop an action plan on standardization of credit derivatives markets by autumn 2009.
- The FSB will develop mechanisms for cooperation and information sharing between relevant authorities concerning hedge funds that will be implemented by the G20 members by the end of 2009.
- The G20 leaders committed to develop proposals, by the end of 2009, to make it easier for developing countries to secure the benefits of a new cooperative tax environment.
- A regulatory oversight regime of credit rating agencies should be established by the end of 2009.
- Guidelines for harmonization of the definition of capital should be produced by the end of 2009.
- FSB, BCBS and CGFS, working with accounting standard setters, should move forward, with a deadline of the end of 2009, the implementation of the recommendations contained in the London Declaration, concerning mitigation of pro-cyclicality.
- The BCBS should review minimum levels of capital and develop recommendations in 2010.
- Further recommendations by the World Bank on voice and representation reforms are expected at the next meetings, which should be agreed by the 2010 spring meetings.
- BCBS and authorities should move forward on improving incentives for risk management of securitization and also develop a global framework for promoting stronger liquidity buffers by 2010.
- The IMF should complete its next quota review by January 2011.

end, measures were introduced to avoid backsliding on the Millennium Development Goals (MDGs) and to provide financing for sustainable development, including:

- Increase of US$50 billion in crisis support for low income countries, including resources for long-term food security.
- Bolster financing options for emerging and developing nations in several ways (see Box 1).
- Provide for a "fair and family-friendly labour market for both women and men," and ensure investments in education and training focused "on the most vulnerable."
- Support the World Bank's Vulnerability Framework, including the Infrastructure Crisis Facility and the Rapid Social Response Fund, through voluntary bilateral contributions for social protection.

At the L'Aquila G8 Summit, the leaders agreed to:

- Strengthen the G8's accountability with respect to the G8 commitments "with regard to development and development-related goals."
- Significantly change investment patterns that will accelerate the transition towards low-carbon and energy-efficient growth models, and, moreover, an urge to keep global average temperatures under two degrees above pre-industrial levels.
- Work collectively towards Copenhagen to develop a "willingness to share with all countries the goal of achieving at least a 50% reduction of global emission by 2050" and to support the "goal of developed countries reducing emissions of greenhouse gases in aggregate by 80% or more by 2050."
- Put food security on the core summit agenda. Concerning the growing trend of international agricultural investment (countries buying land especially in African countries), the leaders agreed to work with partner countries and international organizations to develop a joint proposal on principles and best practices.
- Introduce macroeconomic measures to minimize the consequences of the crisis on the labour market.
- Improve the sustainable access to water and sanitation and to promote health-related topics.

Box 3: Autumn 2009 Economic Meetings

- G20 Trade Ministers Meeting on Doha Round
    - September 3-4, New Delhi, India
- G20 Finance Ministers and Central Bank Governors Meeting
    - September 4-5, London, United Kingdom
- G20 Leaders Summit
    - September 24-25, Pittsburgh, United States
- Annual Meetings of the World Bank and IMF
    - October 6-7, Istanbul, Turkey
- G20 Finance Ministers and Central Bank Governors Meeting
    - November 7-9, Scotland, United Kingdom
- 17th APEC Economic Leaders Meeting
    - November 14-15, Singapore
- WTO Ministerial Conference
    - November 30 - December 2, Geneva, Switzerland
- UNFCCC COP-15 Climate Conference
    - December 7-18, Copenhagen, Denmark

Box 4: Outstanding Issues for the G20 Pittsburgh Summit

- Financial sector controls: Coordinated controls of the financial sector, agreed upon at London, must still be implemented. Systemic financial stability regulators may be proposed to enhance cross-border coordination.

- National regulatory schemes: Divergence is materializing, on a global scale, on issues; for example, on credit rating agencies, hedge funds, regulation of derivatives and compensation for bankers.

- Hedge funds regulation: Despite the IOSCO proposed measures, there is still no agreement between the countries on how exactly it should be implemented — some countries push for a stronger regulation than IOSCO's recommendations. Especially the question of how extensively to regulate hedge funds.

- Elimination of toxic assets: The coordination to manage the problem with toxic assets is not solved yet. Stress tests in the United States are not yet completed and other countries must also do so.

- Bank Bailouts: The "too big to fail" conundrum remains an open discussion.

- World currency: China, India and Brazil may push for comprehensive discussions of a supranational SDR-based reserve currency.

- Reform of the IMF: This remains an open and pressing issue, in content and form.

- Reform of the World Bank: In tandem with discussions of more funding, a review of the Bank's governance remains an open issue.

- Conclusion of the Doha Round: Further movement towards a conclusion of the WTO Doha Round and reaction to the meeting of the trade ministers shortly before the Pittsburgh Summit.

- Climate-related provisions: Pittsburgh will provide an opportunity for common approaches to carbon tariffs and carbon leakage ahead of the Copenhagen climate conference.

- Exit strategies: While G20 countries agreed on the mitigation of pro-cyclical fiscal measures, their resolve will be tested as recovery begins. At Pittsburgh, hidden dangers in the winding down of national stimulus programs may be exposed.

ii. G20 Calls on Other Institutions

At London, the G20 called on other institutions to address the MDGs, development assistance and climate change. The communiqué tasked the following:

- The UN shall, in cooperation with other global institutions, establish an effective mechanism to monitor the impact of the crisis on the poorest and most vulnerable.
- In order to reform the Debt Sustainability Framework, the IMF and World Bank are called on to report in the next Annual Meetings. The International Labor Organization is called on to assess required future actions.
- Concerning climate change, the MDBs are encouraged to contribute to the transition towards clean, innovative, resource-efficient, low-carbon technologies and infrastructure.
- The World Bank and other MDBs are encouraged to use their full capacity in support of their development agenda.

Among the declarations made at Washington, London and L'Aquila, the Financial Action Task Force (FATF) was called on to review its process for assessing compliance by jurisdictions with anti-money laundering and combatting the financing of terrorism. The G8 also called on the FSB to asses jurisdictions against international supervisory and prudential standards. The FATF and the FSB were both tasked to report on their progress by September 2009.

Annex II: CIGI Projects Spotlight

CIGI'09: Towards a Global New Deal

Every autumn, the Centre for International Governance Innovation (CIGI) hosts its annual conference. This landmark event brings together accomplished researchers, policy makers, business leaders and journalists to identify and debate issues of critical importance and to explore innovative practices that can assist in addressing global challenges.

This year's conference, *CIGI'09: Towards a Global New Deal* (October 2-4, 2009), will address the systemic impacts of the current global economic crisis and the long-term prospects for international governance. *CIGI'09* will bring together more than 200 internationally recognized speakers, panelists and participants to address and debate the following broad themes: 1) The impact of the current global economic crisis on the evolution of various governance systems; and 2) The future role of financial regulators, the evolving role of the state in economic governance, and views on whether globalization should be furthered or better harnessed in light of the crisis.

Panelists will discuss the themes in relation to the effects of the crisis on global finance, trade and investment, food security and poverty, and potential environmental challenges. The role of leadership will be a central issue throughout the conference, and will be discussed in-depth during the panel "Future Global Economic Leadership." This panel will focus on the interaction of institutions, government and non-state actors in the leadership of the global economy.

For more information on CIGI'09, agenda, participants and conference report, please visit: www.cigi09.org

Study Group on Global Economic Governance

The global economic crisis has helped to expose significant gaps in the international financial system. While present efforts have focused on the regulation of systemically important institutions, markets and products, major challenges such as institutional reform, currencies and macro-level imbalances loom unaddressed over international debates. In November 2008, CIGI partnered with Chatham House and Istituto Affari Internationali for a two-year examination of the long-term implications of the crisis for the structure and operation of global economic governance.

The Study Group has assembled international scholars and experts to analyze the G20 process, to track national and international policy responses, and to provide recommendations for reform of the global financial and monetary architecture. As an extension of the Economic Diplomacy stream of CIGI's BRICSAM research project, the Study Group pays particular attention to the role of the major emerging powers and to the reform of international financial institutions to reflect the shifting economic order. Through this analysis, the Study Group examines post-crisis scenarios and proposes adaptive structures for responsive economic governance.

A special issue of *International Affairs*, entitled "Global Economic Governance in a World of Crisis" (May 2010), has been commissioned alongside a set of joint CIGI-Chatham House briefing papers on key issues for G8/G20 deliberations. Study Group members have been accredited for each of the Washington, London and L'Aquila summits and will attend the Pittsburgh Summit, and have engaged core constituencies in wider debates on the international financial architecture.

GLOBAL TRADE ALERT

The global economic downturn has seen the collapse of banks and industry sectors, and rising unemployment. Governments en masse have introduced massive stimulus packages, bailouts and subsidies to kick start their own economies and by extension the world's economy. Many of these packages include protectionist measures that, according to the World Trade Organization's General Council, are increasing tensions between nations.

Global Trade Alert is a new online resource that monitors policies affecting world trade, coordinated by the Centre for Economic Policy Research (CEPR) and a consortium of international research institutes, including IDRC, the World Bank and CIGI. An independent initiative, Global Trade Alert provides real-time information about measures taken by governments during the global economic downturn and their likely effects on foreign commerce. Member research institutes identify and assess how these new state measures will impact trading partners.

The up-to-date information and informed commentary provided by Global Trade Alert will help ensure that the G20 pledge not to "repeat the historic mistakes of protectionism of previous eras" is met, by maintaining confidence in the world trading system, deterring beggar-thy-neighbour acts, and preserving the contribution that exports could play in the future recovery of the world economy. For its contribution, CIGI has drawn on its extensive network of scholars and think tanks worldwide to provide concrete policy advice and monitoring.

For more information, or to review the Global Trade Alert's analysis, please visit: www.globaltradealert.org

NATIONAL PERSPECTIVES ON GLOBAL LEADERSHIP

The National Perspectives on Global Leadership (NPGL) project is a collaborative effort between CIGI and the Brookings Institution's Global Economy and Development Program which aims to generate a stimulating inquiry into various economic, political and international dimensions of national and global leadership as manifested in summitry. NPGL's research assesses the degree to which a broader summit grouping – in the context of the global economic crisis – can restore confidence and trust in the capacity of national leaders to overcome economic obstacles.

Drawing on the network of think tank scholars, experts and former officials of CIGI's Breaking Global Deadlocks project in G20 countries, NPGL seeks to advance the idea of a "global steering committee" by fostering ongoing dialogue and relationship-building between key global actors. Through CIGI's website, NPGL provides analysis of national perspectives on a series of specific policy areas, as revealed in national media outlets in the run-up to and immediate aftermath of major summits. These short studies are contributed by participating think tank experts from Argentina, Brazil, Canada, China, France, Germany, India, Mexico, South Africa, Turkey, the UK and the US, and are structured to provide comparable analyses of each country's outlook on global economic leadership.

NPGL advances understandings of the important global issues while also contributing to the development of stronger communications and confidence-building relationships among G20 countries. To review all commentaries from the G20 London Summit and the G8 L'Aquila Summit, please visit: www.cigionline.org

Contributors

Alan S. Alexandroff

Alan S. Alexandroff is a CIGI senior fellow and research director of the Program on Conflict Management at the Munk Centre for International Studies at the University of Toronto.

Colin I. Bradford, Jr

Colin I. Bradford, Jr. is a CIGI senior fellow and non-resident senior fellow at the Brookings Institution.

Barry Carin

Barry Carin is a CIGI senior fellow and associate director of the Centre for Global Studies at the University of Victoria.

Gregory T. Chin

Gregory T. Chin is a CIGI senior fellow and assistant professor of political science at York University in Toronto.

Andrew F. Cooper

Andrew F. Cooper is CIGI's associate director and a distinguished fellow. He is a professor of political science at the University of Waterloo.

Eric Helleiner

Eric Helleiner holds the CIGI chair of international political economy at the Balsillie School of International Affairs. He is a professor of political science at the University of Waterloo.

John F. Helliwell

John F. Helliwell is a member of CIGI's International Advisory Board of Governors and is professor emeritus of economics at the University of British Columbia.

Thomas Homer-Dixon

Thomas Homer-Dixon holds the CIGI chair in global systems at the Balsillie School of International Affairs. He is a professor in the Centre for Environment and Business in the Faculty of Environment at the University of Waterloo.

Jennifer A. Jeffs

Jennifer A. Jeffs is a CIGI senior fellow and president and CEO of the Canadian International Council.

Bessma Momani

Bessma Momani is a CIGI senior fellow and an associate professor of political science and history at the University of Waterloo.

Daniel Schwanen

Daniel Schwanen is CIGI's deputy executive director (programs).

Pierre L. Siklos

Pierre L. Siklos is a CIGI senior fellow. He is a professor of economics and director of the Viessmann European Research Centre at Wilfrid Laurier University in Waterloo.

Gordon Smith

Gordon Smith is a member of CIGI's International Advisory Board of Governors and executive director of the Centre for Global Studies at the University of Victoria.

Debra P. Steger

Debra P. Steger is a CIGI senior fellow. She is a professor in the Faculty of Law (Common Law) at the University of Ottawa and leader of the EDGE Network Projects on Global Economic Governance.

Ngaire Woods

Ngaire Woods is a member of CIGI's International Advisory Board of Governors. She is a professor of international political economy and director of the Global Economic Governance Programme at Oxford University.

Acknowledgements

The editors extend immense gratitude to the contributing authors, without whom this timely initiative would not have been possible. Their dedication and ability to meet short deadlines was matched only by their enthusiasm for the project. The constructive comments of Eric Helleiner, Gregory T. Chin, Ngaire Woods, John Curtis, Ramesh Thakur, Stefano Pagliari and Michael Erdman on the scope and substance of this report are greatly appreciated. Special thanks go to Andrew Schrumm, who managed this project effectively — despite other time pressures — bringing concept to reality. CIGI's publications unit — Max Brem, Jessica Hanson, Joshua Lovell and Tammy McCausland — delivered in a big way, getting the report published at a very busy time. The attractive cover design and layout are a credit to Steve Cross's continued creativity. Finally, the editors thank Thomas Agar, Joe Turcotte and Deanne Leifso for their ongoing assistance.

About CIGI

The Centre for International Governance Innovation is an independent, nonpartisan think tank that addresses international governance challenges. Led by a group of experienced practitioners and distinguished academics, CIGI supports research, forms networks, advances policy debate, builds capacity and generates ideas for multilateral governance improvements. Conducting an active agenda of research, events and publications, CIGI's interdisciplinary work includes collaboration with policy, business and academic communities around the world.

CIGI's work is organized into six broad issue areas: shifting global order; environment and resources; health and social governance; international economic governance; international law, institutions and diplomacy; and global and human security. Research is spearheaded by CIGI's distinguished fellows who are leading economists and political scientists with rich international experience and policy expertise.

CIGI was founded in 2002 by Jim Balsillie, co-CEO of RIM (Research In Motion), and collaborates with and gratefully acknowledges support from a number of strategic partners, in particular the Government of Canada and the Government of Ontario. CIGI gratefully acknowledges the contribution of the Government of Canada to its endowment Fund.

Le CIGI a été fondé en 2002 par Jim Balsillie, co-chef de la direction de RIM (Research In Motion). Il collabore avec de nombreux partenaires stratégiques et exprime sa reconnaissance du soutien reçu de ceux-ci, notamment de l'appui reçu du gouvernement du Canada et de celui du gouvernement de l'Ontario. Le CIGI exprime sa reconnaissance envers le gouvern-ment du Canada pour sa contribution à son Fonds de dotation.

Publications Team

Senior Director of Communications: Max Brem

Publications Coordinator: Jessica Hanson

Media Designer: Steve Cross

Copyeditors: Joshua Lovell and Tammy McCausland

Media Contact

For media enquiries, please contact:

Neve Peric

Media Relations Director

Tel: +1.519.885.2444 x390

Email: nperic@cigionline.org

CIGI

The Centre for International Governance Innovation

Centre pour l'innovation dans la gouvernance internationale

Addressing International Governance Challenges

57 Erb Street West, Waterloo, Ontario N2L 6C2, Canada · tel +1.519.885.2444 · fax +1.519.885.5450 · cigionline.org