While America *Dithered*

The G-20 prospered.

By Barry D. Wood

Amid palpable fear on Saturday, October 12, 2008, President George W. Bush made an unplanned visit to the International Monetary Fund.

Global equity markets were tanking—London and Tokyo were down 10 percent in a day, and $2.4 trillion had evaporated from Wall Street since the failure of Lehman Brothers three weeks earlier. U.S. car companies were approaching bankruptcy. Congress had just approved a $700 billion bank bailout.

The IMF and World Bank meetings were taking place during a meltdown that seemed to herald global recession—or worse.

Bush spent a tense forty minutes with the finance ministers and central bankers from twenty advanced and developing economies, promising a quick response to restore confidence. A global plan of action, he said, would assure that banks had liquidity. Credit would be unfrozen, depositors protected.

Days later after hurried visits from French President Nicolas Sarkozy, then-president of the EU Council, and EU Commission chief José Manuel Barroso, the White House announced that Bush would soon host a summit of leaders of major economies.

The impulsive French leader suggested the emergency summit be held in New York, where he rightly argued the crisis had erupted. Sarkozy wanted the core participants to be the Group of Eight—Europe's four

Barry D. Wood is a Washington columnist and correspondent for RTHK in Hong Kong.

THE INTERNATIONAL ECONOMY
THE MAGAZINE OF INTERNATIONAL ECONOMIC POLICY
220 I Street, N.E., Suite 200
Washington, D.C. 20002
Phone: 202-861-0791
Fax: 202-861-0790
www.international-economy.com
editor@international-economy.com

largest economies, the United States, Canada, Japan, and Russia—whose leaders met each year, plus rising powers China, India, and Brazil.

Refusing to be stampeded and wary of losing the initiative, Bush chose instead to elevate the more inclusive Group of 20, whose economic policy teams he had just consulted at the International Monetary Fund. "We needed something quickly," said a Treasury official. "The G-20 was there and we took it off the shelf."

As a financial entity, the G-20 was the creation of Canada and the United States. In April 1999 in the wake of the Asian and Russian crises, Canadian Finance Minister Paul Martin came to see U.S. Deputy Treasury Secretary Lawrence Summers, who was awaiting confirmation as Treasury Secretary. Martin had long advocated that key developing countries have a bigger say in global economic policy. The two officials proposed that a broad grouping of ministers be formed to share information and monitor global markets.

The rise of the G-20 corresponds to the marginalization of the IMF.

Martin, Canada's prime minister from 2003 to 2006, recalls that the G-20 list was sketched out on a sheet of paper. Adding to the G-8, they sought to balance economic clout with geographic and ethnic representation. They selected the three biggest Latin American economies, Brazil, Mexico, and Argentina, Asian powerhouses China, India, and South Korea, Saudi Arabia because of oil, plus Turkey and South Africa. Their final choice was Indonesia. Nigeria, enmeshed in turmoil during a transition from military to civilian rule, was considered but not chosen. Instead, the twentieth slot went to the European Union.

In IMF affairs, developing countries are confined to an outhouse.

The first G-20 leaders meeting, officially, "The Summit on Financial Markets and the World Economy," took place over a twenty-four-hour period in Washington on November 14 and 15, 2008. Following a White House dinner, the leaders convened Saturday morning along a large rectangular table in the cavernous atrium of the nineteenth-century National Building Museum near the U.S. Capitol. The summit concluded shortly after midday.

A CRITICAL HANDOFF

Thus occurred the critical handoff from the Eurocentric G-8 (Russia had been added to the G7 in 1998) to the new G-20 as the steering committee of the global economy. The expanded group brought legitimacy and inclusiveness to the G-8. Collectively, G-20 nations account for 85 percent of global output, 75 percent of trade, and two-thirds of the world population. With China, India, and Brazil added to the club, the G-20 instantly became a force to be reckoned with.

Jim O'Neill, former top official at Goldman Sachs, calls the creation of the G-20 "one of the few positive consequences of the financial crisis. …[I]t is a far more representative forum for international leadership than the old G-7 ever was."

The Washington Summit prompted a flurry of coordinated crisis responses to halt and then reverse the global downturn. Finance ministers were ordered to present specific measures at a follow-up summit to be held within four months.

In the United States, a presidential transition had been underway. President-elect Barack Obama stayed away from the Washington Summit, but his economic team moved swiftly, endorsing the process and preparing for what would be the London summit in April 2009.

Fred Bergsten

Silent G-2

Fred Bergsten of the Peterson Institute says that China in a G-7 would wreck the G-20, as the remaining leaders would view their grouping as second class. Bergsten likes what he calls a silent G-2 of China and the United States, which he says tacitly exists as the Chinese and American leaders have been meeting multiple times each year.

—B. Wood

At London, the leaders agreed to coordinated measures that made that gathering the showpiece of the G-20 process thus far. Fiscal stimulus packages totaling $5 trillion were unveiled. The leaders pledged resistance to trade protection and competitive currency devaluations,

The creation of the G-20 was "one of the few positive consequences of the financial crisis."

aware that beggar-thy-neighbor policies disastrously worsened the Great Depression. They pledged an additional $1 trillion to the IMF to make sure the financial agency had what it needed to assist distressed members. They elevated the Financial Stability Forum to the Financial Stability Board, assigned with the task of harmonizing regulatory and supervisory policies.

"MOST IMPORTANT MEETING IN TWENTY YEARS"

Larry Summers, by then a top Obama Administration official, calls the London Summit "the most important economic meeting in twenty years." It averted catastrophe and laid the foundation for recovery. Paul Martin agrees. "The coordinated stimulus and other measures," he says, "prevented the financial crisis from becoming a global depression."

The new G-20 club met a second time in 2009, at Pittsburgh in November. The leaders met twice in 2010 (Toronto and Seoul), and then as the crisis diminished scaled back their meetings to once a year (Cannes 2011, Los Cabos, Mexico, 2012, St. Petersburg 2013, Brisbane, Australia, 2014). This year's November 15–16 meeting in Antalya on Turkey's Mediterranean coast will be the first G-20 in an Islamic country. China will host the 2016 meeting.

The challenge the G-20 faces, says Fred Bergsten of Washington's Peterson Institute for International Economics, "is shifting from crisis response to systemic management." It must avoid decaying and fading.

To avoid that fate, Bergsten suggests the leaders select a globally significant project to engage policymakers. That, he says, "would maintain the G-20 so that it is there for the next crisis." He offers climate change, immigration, global governance, and investment as project candidates.

Each G-20 summit seeks to balance effectiveness with representation, efficiency with inclusiveness. With the chairmanship rotating among members, the host leader prepares the agenda, chairs meetings, and invites additional guests.

Sometimes there have been too many guests. At Seoul in 2010, there were two hundred people around the table. As the Australians prepared to host the 2014 summit, they were aghast to discover that previous meetings had set seventy-three work streams in motion. The Australians set out to streamline the proceedings, focusing on a single theme—growth—and beginning the one-and-a-half day session with an unscripted informal retreat where leaders were encouraged to speak their minds. In the formal sessions, time clocks limited each leader's remarks.

The Turks have selected three I's as a summit theme: implementation (of the Brisbane growth targets), investment, and inclusiveness.

John Kirton, the University of Toronto professor who heads the G-20 Research Group, believes an extra day should be added to the meetings. "Often," he says, "the leaders fly for a longer time than they meet." Kirton suggests "the leaders get back to work" and meet twice each year, an idea that has found little support.

SUMMERS' LAW

There are differing views about how many members a steering group should have. Worried that the G-20 is too big to easily reach decisions, Jim O'Neill calls for a revamped G-7 that includes China.

Bergsten of the Peterson Institute rejects the suggestion, saying that China in a G-7 would wreck the G-20 as the remaining leaders would view their grouping as second class. Charles Dallara, the former head of the Institute of International Finance, suggests a G-4 of the United States, China, Japan, and the European Union. Bergsten says that, too, is a non-starter because, "the Europeans are unwilling to yield to a single EU representative."

Larry Summers calls the London Summit "the most important economic meeting in twenty years."

Bergsten likes what he calls a silent G-2 of China and the United States, which he says tacitly exists as the Chinese and American leaders have been meeting multiple times each year.

Harvard Professor Larry Summers shrugs, asserting that the financial architecture is flexible enough to accommodate various groupings. He goes on to posit what he calls Summers' law on groups: "Every country," he says, "wants to be in the smallest group and every country likes whatever group it's in."

BOTCHED IMF REFORM

The rise of the G-20 corresponds to the marginalization of the IMF. Every G-20 declaration since 2008 has called for a recalibration of the weighted votes in the IMF to give greater voice to rising powers.

With the Obama Administration taking the lead, the Seoul Summit in 2010 agreed to a 5 percent shift of votes from over-represented Europe to emerging markets. Under the agreement, China would have its voting share rise from 2.9 percent to 6 percent. There would be modest increases for India, Brazil, and others. This initial shift was to be followed by another, which would also revise the complicated formula for determining economic weights.

Liaquat Ahamed, author of a recent book on the IMF, says the current structure in which Belgium has more votes than Brazil, and Belgium combined with Holland more votes than China, is not only outdated but absurd. Jim O'Neill notes that since the quota deal was struck five years ago, China's economy has doubled in size and is bigger than France, Germany, and Italy combined.

The 2010 reforms—which also double IMF resources—have been blocked because of U.S. failure to ratify the package. With 16 percent of the votes, U.S. approval is needed for the 85 percent approval required for implementation.

The IMF measure is hostage to the deep animosity between congressional Republicans and President Obama. John Lipsky, the American former deputy IMF chief, calls the impasse "destructive for U.S. credibility." An executive director from a country friendly to the United States says, "It is impossible to overstate the damage that's been done." Liaquat Ahamed dismisses Republican objections to IMF reform, saying the U.S. contribution "has no budgetary impact … is a 'freebie,' akin to putting money into one's credit union account."

U.S. inaction, says respected economist **Mohammed El-Erian,** *"has left the global economy without a conductor."*

The frustration felt by the rising powers over the IMF governance debacle is huge. An executive board member told me that in IMF affairs, developing countries are confined to an outhouse. In 2012, a Chinese visitor to the boardroom observed to his guest that eight of the twenty-four seats around the table were occupied by Europeans. He asked scornfully, "Is this reflective of today's world economy?" Arvind Subramanian, economic advisor to the Indian prime minister, says it is indefensible that Europe has 30 percent of IMF votes.

Belgium has more votes than Brazil, and Belgium combined with Holland more votes than China.

It has long been argued that nothing gets done in international economics without U.S. leadership. That is changing. Stymied in their bid for a bigger voice at the IMF, the BRICS nations (Brazil, Russia, India, China and South Africa) have organized their own currency reserve arrangement for swapping reserves if one of the five gets into financial difficulty.

O'Neill says the absence of appropriate representation at the IMF "has driven the creation of new parallel institutions such as the Asian Infrastructure Investment Bank and the New Development Bank founded in 2014 by the BRICS."

U.S. inaction, says respected economist Mohammed El-Erian, "has left the global economy without a conductor."

Larry Summers, assessing failed IMF reform and Washington's resistance to the Chinese-led AIIB, fears that early 2015 may be remembered as the time "the United States lost its role as the underwriter of the global economic system."

While the IMF struggles, the G-20 soldiers on doing what Paul Martin says it must do—making globalization successful for all. ◆