

Journal of Globalization and Development

Volume 2, Issue 2

2011

Article 7

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Recommended Citation:

Dadush, Uri and Suominen, Kati (2011) "Is There Life for the G20 beyond the Global Financial Crisis?," *Journal of Globalization and Development*: Vol. 2: Iss. 2, Article 7.

DOI: 10.1515/1948-1837.1244

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Is There Life for the G20 beyond the Global Financial Crisis?

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The G20 summit of heads of state, a creature born of the financial crisis, has appointed itself as the preeminent forum for global economic policymaking. Notwithstanding its original design to curb food price volatility, reform the global monetary system, and improve the working of the G20 itself, the group's latest summit in Cannes, France in November 2011 was hijacked by the prolonged Eurozone financial crisis. An enormous source of turbulence in the world economy, Europe's problems are the world's problems and should be on the G20 agenda. But the Euro crisis also diverted the G20's focus from its long-term imperative: ensuring sustained global economic growth. Instead, the outcome of the summit was inconclusive, vague, and thus modest: the group agreed in principle to increase the resources of the International Monetary Fund to respond to Europe's woes; China modestly strengthened its pledge to move towards exchange flexibility to assuage critics of its currency manipulation; and the leaders yet again expressed their commitment to the Doha trade round.

The French summit epitomizes the difficulties in making sweeping yet specific decisions in a large, diverse group of nations with divergent interests. Comprising ten emerging markets, nine advanced economies, and the EU, the G20 reflects the reality of a world economy where developing and advanced countries are starting to have roughly equal economic weight. By including the largest emerging markets, it has the potential to fill a large gap in global economic governance that its predecessors – the G4 launched by US Treasury Secretary George Schultz in 1973, and the subsequent permutations, G5, G7 club of rich countries, and the G8, which also included Russia – were not built to bridge. The G7 helped the liberal democracies prevail in the Cold War and worked to enhance global macroeconomic stability, while the G8 sought to engage Russia after the collapse of the Soviet bloc. But with the onslaught of economic globalization and the rise of emerging economies, both groups are outdated as venues for global policy coordination. The G20, on the other hand, looks and feels like a 21st century forum.

The G20 is not a new forum: the group has met at finance ministers' level since 1999, after the economic firestorm engulfing the emerging world caused by the 1997-98 Asian financial crisis compelled the treasuries and central banks of advanced economies to engage their counterparts in volatile emerging markets. But it is the G20 leaders' summitry, operational since being organized by the George W. Bush administration in Washington in November 2008, that has started the kind of international conversation that is now necessary – one that involves emerging and advanced countries at the highest level and centers on the thorniest issues in the world economy, from ways to tackle the global financial crisis to coordinating banking regulations and jumpstarting world trade negotiations

Frictions between the members are inevitable: not only are the stakes high; there are differences in expectations, ideas about global governance, and economic starting points. The G20's role is to mediate the differences in order to safeguard the common interest in a growing and stable world economy. On that score, the first few G20 summits were quite promising. The group pledged to stimulate economic activity, overhaul financial regulations, tame global financial imbalances, avoid protectionism, and to greatly expand the lending capacity of the International Monetary Fund to better respond to the crisis (table 1), as well as revise the governance of international institutions.

Initial progress was impressive, most notably, the success of stimulus measures in containing the economic freefall and the avoidance of widespread protectionism. Moreover, the G-20 replaced the Financial Stability Forum, which included only the advanced economies, with the Financial Stability Board that includes numerous emerging nations and is charged with coordinating global financial regulations, and it helped rebalance the executive board and voting quotas of the International Monetary Fund (IMF) in favor of China and other emerging countries while tripling the institution's resources.

However, as the worst of the economic crisis began to dissipate, the consensus for concerted action frayed, and the group's effectiveness fell in doubt. There were many good reasons why. Concerns about global imbalances persisted, new currency tensions emerged, the Doha Round remained dead in water, and tighter financial regulations were fiercely resisted, while progress on coordination was glacial. And instead of keeping its eye on these badly needed long-term reforms, the G20 started falling prey to crises *du jour*: in Toronto, it was the advanced economy fiscal crises that usurped the attention, in Seoul, currency wars hijacked the agenda, and the Cannes Summit was held hostage by the Eurozone crisis.

In light of these challenges, will the G20 be able to deliver on its long-term promise? Will the group succeed at transforming itself from a crisis-fighter to an effective forum of global economic governance – one that helps build the underpinnings of sustained global growth as well as insure macroeconomic stability? Can it remake international institutions into more effective tools for tackling the challenges of the 21st century world economy? The answer could well be positive. But to get to a definite yes, the G20 has to confront four major challenges: build on its comparative advantages, be realistic in what it can achieve, effectively integrate emerging economies in global governance, and clarify its own structure and composition. And it needs leadership from its largest members, beginning with the United States and China, to accomplish any of this.

What Is the G20's Comparative Advantage?

The G20 is not designed to be a decision-making body: its deliberations are not ratified by parliaments and therefore are more statements of intention than binding agreements. Nor is it a universally representative body. The G20 is well-positioned, however, to function like an international board of non-executive directors, or steering committee. It is an avenue of strategic coordination without heavy operational obligations: a leader rather than crafter of detailed rules or executant of projects, chairman rather than CEO. Its flexibility and open-endedness also allow the G20 to react quickly to events. It is therefore well suited to provide general guidance for how the international institutional architecture should evolve, but also for crisis management, where circumstances change rapidly, uncertainties abound, and the treasured prerogatives of national policymaking are at stake.

However, as coordinator-in-chief, the G20 is not well suited to engage at the granular level. The farther it ventures into the weeds, the greater the risk that it loses the authority endowed to it by heads of state, and also that it encroaches on the territory of established multilateral institutions, such as the IMF, World Bank, and WTO, whose technical competence is far greater. In short, the greater the risk of paralysis as it loses both efficacy and legitimacy. Each of the world bodies has its respective idiosyncratic, technical, and contentious work program. Acrimony over any such detailed issues should not be allowed to contaminate the G20's broad agenda, as that would only stifle its decision-making, and disincentivize coordination among the members.

Concerns about the G20 degenerating into a grand photo-op are valid, but the answer is not wading into detail or making each decision binding "hard law". Besides, morphing the G20 into explicit decision maker and executants would antagonize the many nations that are not G20 members – in the case of the WTO, more than 130 nations, and in the case of the IMF, more than 160.

Instead, the G20 countries, which together account for the vast majority of the ownership and voting power in the major global institutions, should focus only on the big picture and look to those institutions to translate the G20-designed strategy into explicit decisions – in other words, to find a technically and politically palatable way to execute and enforce the G20's vision. This is the role – the role of a steering committee – that the G20 needs to continue carving out. It has sometimes used this approach to good effect, calling on the IMF to aid its mutual assessment process aimed at global rebalancing and macroeconomic coordination, the World Bank to develop a template for a new global development agenda, and the OECD, UNCTAD, and WTO to systematically monitor and report on trade and investment protectionism. Similarly, the G20 plan for combating corruption builds on an existing UN agreement.

Realism: Know Thy Weakness

The G20 has unique strengths as a coordinating forum. But its strengths are also its weaknesses. Leaders, as well as the commentators who watch them, must recognize the G20 has limitations and set the agenda and expectations accordingly.

For one, the G20 and its watchers need to differentiate between the forum and its individual members – the issues that multilateral institutions beginning with the G20 can genuinely make progress on and those that depend instead on domestic political processes in the largest economies on which the G20's influence is remarkably limited, while disagreements are rife.

The drive to tame global imbalances epitomizes the problem. Needing exports for growth and employment, China and Germany disagree with the United States, UK, and other deficit nations on the G20's rebalancing effort. Moreover, global imbalances are largely the reflection of domestic forces, for example, financial repression and structural constraints to boosting consumption in China, and political differences on how to reduce the US budget deficit.

Unsurprisingly, the G20 has thus far had little success in agreeing on a roadmap to effectively deal with global imbalances, and has also failed to set a clear goal for its efforts. Imbalances, like other issues on G20's agenda, hinge on domestic reforms in the leading economies, but they have been branded as "global" and therefore put front and center of the group's agenda. Yet the reality is that none of the large G20 economies will correct the drivers of the imbalances – China pushing for domestic consumption or the United States defusing its fiscal time bomb – unless domestic politics align and such actions are in these nations' self-interest. They will not do so just because the G20 decided these might be global desirables, and the group should either find a way to focus on domestic reforms, or avoid placing such a high stake on the quick resolution of global imbalances.

The G20's record in general has been uneven. A recent report by the G20 Research Group, which reviewed the period from November 2010 to June 2011, found that the G20 members have a 70 percent compliance rate on 13 priority commitments made in the Seoul summit, better than a compliance rate of 64 percent in the Toronto summit and 62 percent in the Pittsburg summit (Montpetit 2011).

But there is Achilles' Heel: of the 13 commitments assessed from the G20 Seoul Summit, only one, fiscal consolidation, received a perfect compliance score (i.e., all nations complied); eight items, such as exchange rates, OTC derivatives, international development, and clean energy cooperation, were partially complied with, while commitments on "international cooperation" — closer coordination between the G20 and the United Nations, regional bodies, civil society, trade

unions and academia — has one of the lowest scores, as does international trade, where the G20 has failed to meet its repeated early pledges to refrain from new protectionist actions and conclude the Doha Round. While the methodology can of course be questioned, overall, the highest compliance scores went to Australia, UK, France, and Italy, and Canada; the lowest, to Argentina, Saudi Arabia, Turkey, and South Africa.

While coordination failures are ancillary to the main problem — that resolution to issues facing the G20 often requires painful domestic reforms — they risk becoming a means to deflect attention from the very domestic reforms that are so badly needed. The coordination that has been accomplished is also not always what it seems: members have at times committed to what they have already decided to do at the domestic level anyway, and then posed their actions as international cooperation. One example was the G20 commitment in the June 2010 Toronto summit to halve government deficits by 2013 and stabilize debt loads by 2016.

The troubles surrounding rebalancing, Doha, and global growth have caused deepening consternation about the effectiveness of international institutions and the G20 in particular. But although the G20 can and should discuss such troubles, it would be unfair to measure its success solely or mainly by their resolution. One has to distinguish between the need to improve the rules of the game and the need for key players to raise their game, not confuse the latter with the former. Lacking enforcement tools, the G20 cannot induce action; it can however shed light on, scrutinize, and monitor its members' policies, and bring global attention to, and pressure on, the misbehaving members that jeopardize the growth and stability of others.

The frustrations with the G20 have naturally led to the familiar calls for enforcement. But enforcement mechanisms are a pie in the sky. With the exception of trade barriers which come under the purview of WTO dispute settlement, all main issues on the G20 agenda to date fall under governments' guarded levers in domestic politics — regulatory, monetary, exchange rate, and fiscal policies as well as official aid — rendering enforcement all but impossible. Moreover, even if it was magically agreed upon, enforcement could stifle the policy debate, as leaders would become much more hesitant to discuss policy options and make any commitments if they know they are to adhere to each word. And if they wouldn't: would the G20 really be able to agree on a punishment mechanism?

But despite its lack of means to drive its decisions through, the G20 can aim to develop broad consensus on the approach to take on global issues, nudge the executives in member states to new directions, and provide political cover for policy change at home. The intangible value of the leaders of the main economies regularly coming together to discuss global economic challenges, let alone the

exchanges among national working groups that precede the summits, should not be underestimated. At the minimum, it promotes a better understanding of each other and the personal relations that are built will enhance responses to the next crisis.

In short, the G20 itself must be aware of its limitations, and not make lofty commitments on agendas it cannot deliver on. It has done so, for example issuing pledges through the October 2009 Pittsburgh Summit to seek to conclude the Doha Round by the end of 2010. As in many previous G7/8 declarations, unaccomplished missions, and the image of the G20 as an effective forum for global governance is tarnished. The G20 should not be expected to run the world, namely overhaul the policies of sovereign nations; rather, it is to prod greater alignment of national policies with the broader interest and to seize the opportunity to produce self-enforcing agreements. That will take consensus building as well as hard bargaining, and therein lies the group's worth.

Getting the Emerging Economies to Dance Along

As Stewart Patrick argued in *Foreign Affairs*, as a diverse forum composed of advanced and emerging nations, the G20 creates the possibility of shifting coalitions that cut across developing and advanced country lines. Such new marriages of convenience have already been made, and the G20 working groups illustrate further possibilities: each is co-chaired by representatives of an advanced and an emerging country, and each aims to tackle a potentially divisive issue, such as imbalances, climate change, and food security. This gives both emerging and advanced nations the opportunity to develop big reform ideas and achieve buy-in among their respective constituencies.

However, some commentators suggest that including emerging countries as full participants will limit the G20's effectiveness. As the emerging powers demand more voice in international organizations, the argument goes, they may resist taking on the associated responsibilities. For example, because improving the much lower living standards of their citizens' is their overwhelming priority, emerging nations are reluctant to undertake any commitments that sacrifice growth. Furthermore, the argument goes, even as these countries look to make their mark on the world stage, they are reluctant to yield sovereignty, even at the cost of torpedoing the international consensus. As a result, international coordination and agreements will inevitably become more circumscribed.¹

There is truth to these claims. Although a member of the IMF and the World Bank, China has long lent to developing nations without the conditions for good economic governance demanded by the multilateral bodies – yet with a

¹ Patrick 2010.

condition to access the recipients' raw materials and secure some degree of political acquiescence. In 2009, China maneuvered with India, Brazil, and South Africa to limit the reach of the global climate change agreements in Copenhagen. Beijing's announcements of RMB appreciations appear to coincide nicely with G20 summits, which helps China deflect attention from its disagreeable currency and other policies. Furthermore, resistance to liberalization in manufactures and services by China, India, and Brazil helped perpetrate the deadlock in the Doha Round in July 2008. And at the April 2011 IMF governors' meetings, emerging nations staunchly opposed proposals to define parameters for legitimizing certain kinds of capital controls and thus effectively barring the use of others. As suggested by the compliance scores compiled by the G20 Research Group, the compliance of several developing country members with G20 decisions has been among the worst in the group.

It would be disingenuous to claim, however, that advanced economies are the paragon of global coordination. They too have often resisted or fallen short of meeting international commitments, including on trade, fiscal policy, and climate change. They also sport long-standing policies, such as agricultural protection and subsidies aimed at catering to special interests, that create distortions in the global economy and the advanced nations themselves. It was the advanced economies that were the epicenter of the global financial crisis, a fact that made countless commentators call for these traditional stewards of global affairs to dismount their high horse and stop preaching responsibility to the emerging players. Indeed, it was smaller advanced economies like Canada as well as the emerging Asian economies that seemed to have the kinds of tools, such as sturdy bank reserve requirements, that are now seen as having cushioned against the storm. The question now is whether learning occurs in the advanced world to remedy the mistakes and not repeat them.

But it is also the case that emerging economies have often been short-sighted and have much learning to do. Some of that learning can occur through peer pressure. For example, with most emerging economies as uneasy as the United States about the ascent of China and Beijing's currency, trade, and foreign policies, intellectual property rights violations, and flailing product standards, the United States has a chance to convince these rising nations that managing the rise of China requires them to invest in the rules-based international order (Suominen 2012). Washington must also avert fissures in the Western alliance and persuade Europeans to work much more vigorously in prodding China and other emerging nations.

Some of the learning comes over time as the game is played. Not only do emerging nations need to learn to play with the advanced economies in developing meaningful, constructive summit agendas; they will have to think through what exactly they themselves want beyond the increased international

influence they covet. As a former Indian WTO Ambassador recently wrote, “The emerging economies cannot continue to hide in the crowd...they will have to step up to the plate and display leadership to take the multilateral process forward. There is little evidence of that at present...”²

To be sure, one recent show of constructive, positive force by the BRICs was their willingness to channel funds to ailing Europe via the IMF – provided Europeans themselves did enough to help themselves, and also swallowed a bitter pill, the use of funding facilities designed for poor economies. However, emerging economies, beginning with China, have so far failed to articulate a clear vision of the specific policies they want to drive on the global stage. And all of them, including China, have to learn to contend with domestic divisions on these issues – including on the very legitimacy of the Bretton Woods institutions and multilateral framework of global governance. For example, some in China still see the current setup as a threat and a means for the West to encircle China, while others see it as more benign, and still others consider it primarily as a useful framework for driving Chinese interests.³

Unlike the United States, which acting in its own enlightened self-interest has supported such global public goods as an open trade regime during the post-war era, and successfully advocated their adoption as the norm, even the largest emerging economies prefer to free ride or to voice their displeasure without articulating an alternative vision. Indeed, emerging economies such as China and India now worry about the flailing US leadership, in part at least because they find themselves unable or unwilling to step up to the plate.

Granted, it is important to make distinctions among the emerging economies, just as among the advanced countries. For example, the November 2010 summit host Korea acted as an effective interlocutor between the advanced and emerging economies as well as non-members and has been a responsible stakeholder on the world stage. Mexico, host of the 2012 G20 summit, is working to rise up to the par. The point is international negotiations require tit-for-tat – yielding on some issues to get one’s way on those issues that matter more. To play this game, the main emerging economies need to establish a clearer ordering of their various preferences and interests.

Of course, such measures would not guarantee better coordination. The challenge is that among the G20 are countries of widely different starting points and interests. Although only the largest G20 nations have a real say on the group’s agenda and outcomes, the kind of coordination of likeminded, developed countries the G7 could pursue is much harder today.

² Ujal Singh Bhatia, “Sources of the WTO’s impasse,” VoxEU.org, 11 May 2011.

³ David Shambaugh, “Beijing: A Global Leader With ‘China First’ Policy,” Yale Global, 29 June 2010 <<http://yaleglobal.yale.edu/content/beijing-global-leader-china-first-policy>>.

In the multiplayer, multi-interest G20, someone has to coordinate the play. And the role of leadership still falls on the United States, the world's largest economy and most powerful nation which as the founder of the post-war system, including the various incarnations of the G summitry, has the longest experience and the largest vested interest in the existing system, and which originated many of the G20's first policy commitments.⁴ Europeans are divided among themselves, Japan crisis-worn, and none of the emerging economies either able or willing to lead. Washington needs to cut the budget deficit, pursue global trade liberalization more assiduously, and ensure the viability of the dollar, for starters. The call on the United States is clear, but whether it will respond remains an open question.

Bigger Table?

As a gathering of heads of state of economies accounting for some 80 percent of world GDP, the G20 seems well positioned to fill its role. However, some argue that it is too large to be effective, while others, including thoughtful leaders in such non-member nations as Denmark or Chile, question the legitimacy of the self-appointed G20. To play its strategic role in global economic policy, the G20 must strike the balance between bringing too many countries and institutions to the table and being too small to be representative.

Catering to the concerns about "international legitimacy" would only lead to ineffectiveness.⁵ The G20 already includes the heads of the IMF and the World Bank and various observers, and as such borders on being too unwieldy. It is also taking on too many issues at once, from climate change to international development, which risk diluting its focus. At the same time, ultimately power on the international stage, rather than numbers, determine who will call the shots. In the final analysis, it is the 5-6 largest G20 members that are in charge, and including another economy the size of Argentina will not change that fact.

To improve continuity and build institutional memory and capacity, policymakers and analysts have aired proposals to establish a G20 permanent secretariat and a more durable presidency. The current set-up – a rotating secretariat and annually rolling presidency, including a "troika" arrangement whereby the previous and successive year's president countries help set the agenda – is not ideal, but it is not clear that any alternative, such as the IMF model of national groupings headed by rotating chairs, would be preferable. It would perhaps add to legitimacy, but also dilute the big-nation summit atmosphere, and reduce the likelihood of creating personal bonds among leaders.

⁴ Suominen (2012).

⁵ Dadush and Shaw (2011)

A longer presidential term would also give one nation too much weight as the 19 others would wait for their turn for years. And while a permanent secretariat would lead to more continuity, it would also, once established, increase the risks of bureaucratization, mission-creep and competition with other institutions. Making the group's work seem more formal could only discourage members from addressing some of the more difficult policy issues.

Conclusion

As the crisis began spreading across the globe, the G20 helped avoid descent into a second Great Depression. It marshaled the large economies to coordinate their stimulus programs, assigned the IMF a large role in carrying out rescues, and helped avert egregious protectionism. On that alone, the institution's balance sheet is positive, and at a minimum it will continue to provide insurance against the next financial crisis. Though it is hard to discern how many of these positive outcomes owe to the G20 and how much would have happened anyway, the group clearly demonstrated its usefulness in crisis. It has also shown glimpses of its longer-term potential – revising the roles and structures of major institutions and setting the global economic agenda. If it avoids the pitfalls of overpromise, overreach, and bureaucratization, and bridges advanced and emerging countries' interests, it can establish confidence in the new world order and help build a viable economic architecture for the 21st century.

The G20 must first and foremost avert the temptation to be all things to all nations and instead keep its eye on the ball – the systemic global policy issues short- and long-term- that affect all nations and where major coordinated reforms are needed. Though global imbalances and currency tensions are rightly part of the discussion, the emphasis should be on highlighting and dealing with the domestic policy failures that are the real cause of the pattern rather than look for illusory solutions in new international monetary arrangements or for quick fixes from the mutual assessment process. Strengthening the world trading system will take much more than another pledge to conclude Doha: a reform of the WTO and its negotiations modalities. Much work also remains to be done to establish the broad common principles on financial regulation so as to avert arbitrage and work together when multinational banks start failing. These core issues must be set right before the agenda is broadened further.

Much will have to get done by each member, at home. While economic linkages have become global, economic fixes are local. Going forward, Europe and the United States must look deep within, much like emerging markets had to do in facing up to their crises (Suominen 2011). The cost of the Eurozone's common currency is greater fiscal integration and enforcement regime; the price for future economic dynamism is flexible labor markets and curtailed welfare

states. In America, the failure of the budget super committee to reach agreement only increased the urgency to free the world's leading economy from its exploding debt load.

And yet, getting to growth in the interdependent modern world takes far more give-and-take. China, India, Brazil and other emerging market economies know that advanced nations' recovery and global rebalancing are in their economic self-interest, but now must act on that understanding. By paving the way to growth, they would show the global leadership they seek – which, after all, is not about new seats in international institutions, but about stepping up to the plate at the world's hour of need.

As it faces up to the global challenges, the G20 must avoid becoming a white elephant, the fate of all too many international endeavors. Repeated failures by the G20 to meet its commitments on rebalancing, the Doha Round, financial regulations, and other policy areas will quickly chip away at the group's credibility and relegate it to irrelevance. The leaders should not underestimate such a prospect.

The key factor between success and failure is leadership. Just like the G5 or G7, the G20 requires leadership for generating useful policy ideas and building support for action around them. And just like in the past, there are only a handful of members that can swing the big decisions. Of those, the United States is still by far the most important and the only plausible leader. And as in the past, it leads best by example and vigor of its economy. On that score, it now has a long way to go.

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