G20’s three steps towards strong, sustainable and balanced growth of the world economy

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First and foremost, I would like to endorse the proposal by Mike Callaghan, the Program Director of the G20 Studies Centre of the Lowy Institute, earlier this year that strong, sustainable and balanced growth (SSBG) should become the overall narrative guiding the whole G20 process, so as to make it easier for the forum to communicate and act. By elevating the SSBG narrative, different hosts would not need to seek different ‘key words’ for their years in the Troika, though the yearly emphasis could evolve in step with the development of the world economic situation. As a way of increasing transparency and simplicity, the G20 members should also consider improving the forum’s website, or establish a virtual secretariat (for example, the BRICS summit has recently launched an online initiative). Up until now, the G20 website has been established and maintained by the host every year, and much of its content has been lost between the transition from one president to the next. A more sustainable model would allow the G20’s online presence to be more like APEC, with one logo and one well-organised website, if not a secretariat.

This paper aims to describe how the SSBG mandate of the G20 should play out in three main areas – namely, crisis prevention, crisis management and long-term growth. The paper concludes with ‘some fuel for thought’ for future G20 hosts.

Financial regulation has being strengthened post 2008; this, however, is not a guarantee of a crisis-free world economy in the future. Since the advent of the G20 leaders’ summits, the G20’s most prominent achievement has been in the strengthening of financial regulation – for example, institutionally, the Financial Stability Forum (FSF) was relaunched as the Financial Stability Board, a fully-fledged international organisation replete with its own bureaucracy. In terms of regulatory standards, old rules (such as the Basel III rules on capital requirement) were discussed and updated, and new rules (such as those relating to OTC and shadow banking) were created or proposed so as to expand the coverage of regulation. Special attention has been paid to systemically important financial institutions (SIFIs), so as to solve
the ‘too big to fail’ issue. The IMF also strengthened surveillance of the financial sectors of its member countries.

However, whether this ‘revolution’ can prevent the next crisis remains uncertain. First, the full implementation of these updated standards may be problematic. The emerging economies have been the most serious in implementing the Basel III accord, while the cross-Atlantic major powers, where the most recent financial crises originated, are lagging behind. Second, it is still not known whether these standards are fully appropriate, complete in scope, or substantively ‘healthy’ for real economies. Third, one of the major risks for the world economy in future decades will come from sovereign debts, while regulating governments will remain a kind of ‘mission impossible’. The way in which major economies like the United States, the EU and Japan unfold their monetary policies will impact the dynamics of the international capital market tremendously. The Mutual Assessment Process (MAP) is meaningful in enhancing communication between these major economies, but minimal in binding their hands. For example, the dominant player, the United States, did not mention its monetary and exchange rate policy in its submission to the MAP framework outlined at St Petersburg.3

Building more reliable firewalls for the world economy is increasingly necessary for global economic governance. Capital is like a genie that was released from its magic bottle in the 1970s. Financial crisis is almost a force majeure that we are unable to overcome in this highly globalised but sovereign world. As people choose to buy more insurance products to prepare for increasing uncertainties, the world needs to reinforce the global financial firewalls. In a similar vein, when Jean Pisani-Ferry, former director of Bruegel, talked about the future direction of the euro area, he emphasised a monetary union with the protection of a financial safety net, rather than a more centralised fiscal union.4

The G20 has already done a lot of work in this area. The firepower of the IMF and World Bank have been tremendously enhanced through quota reform (though the reforms have not fully come into effect yet) and expanded lending arrangements. However, regional financial arrangements (RFAs), including bilateral currency swaps, are proliferating at a faster pace. How to combine the IMF’s knowledge with RFA resources is a key issue in safeguarding the global economy. The 2010 Seoul G20 summit proposed the concept of a global financial safety net, which led to the G20 Principles for Cooperation between the IMF and RFAs, endorsed by the G20 Finance Ministers and Central Bank Governors in Oct 2011. A high-level seminar on the subject was held during the Russia presidency in 2013, based on an IMF stocktaking paper.
The six G20 principles and the IMF stocktaking were a useful starting point for coordination. However, more detailed follow-ups are needed. Among others: first, bilateral swaps should be included in the analysis, considering their size and increasing use. Second, priority should be given to those RFAs being established by emerging economies, such as the BRICS Contingent Reserve Arrangement (CRA), expected to be effective at the 2014 BRICS summit in Brazil, for the following reasons:

- with the expectation of a US withdrawal from quantitative easing, emerging economies (including Brazil, India and South Africa) will be most affected. Good design will be needed to make the CRA operational, taking into account the lessons of the Chiang Mai Initiative Multilateralization (CMIM), which has kept growing but has never been utilised.

- ex ante communication between IMF and CRA will make cooperation smoother, including co-financing and co-analysis. Assurances as to the breakdown of responsibilities between the IMF and CRA need to be well-prepared well in advance of any financing initiative.

- good coordination between the IMF and CRA will have wider implications as a showcase for mutual complementarity, instead of confrontation, between BRICS and existing institutions.

For long-term world economic development, the G20 needs to continue dealing with several outstanding issues.

**Financing for investment**

This is a core issue in job creation, innovation, long-term development and climate finance, among other things, as well as a fundamental way of preventing crisis. The isolation of virtual economy from real economy has gone too far everywhere, leading to the co-existence of ‘money abundance’ and ‘money scarcity’. Like human beings, capital has the dual nature of devil and angel. What we need to do now is to transform the devil into an angel by channelling the flooding capital in the financial sector into the very dry real economy more effectively.

Sergei Storchak, the Deputy Finance Minister of the Russian Federation, commented that the most impressive result during the Russian presidency was that all G20 members agreed to start an active search for alternative sources of investment financing. G20/OECD High-level Principles of Long-term Investment Financing by Institutional Investors was published and
updated. In my opinion, this represents a real shift in the G20’s role from a crisis management agency to a long-term growth steering committee.

Problems are common, but the reasons are very diverse. For some G20 members, limitations might lie in the inefficiency of their respective financial sector, for example, China’s interest rate controls and its limited market access; for others, such as many developing countries, ineffective government might be the bottleneck; for some developed countries, incentives might need to be better regulated. What the G20 should do next is maintain the momentum of its discussions on these issues and translate the principles on paper into action, through encouraging ministers to share experiences, best practices and lessons from their countries, and finding tailored solutions for each.

**Preserving the global open trade system**

The world is experiencing a new round of regionalisation, with deeper penetration and a wider coverage of markets than the WTO. This has caused great concern about the fragmentation of the global trade system, such that it has been placed on to the G20 agenda. What should the G20 do? Certainly, it should stress the value of a multilateral system. The joint research by the OECD, WTO and others regarding global value chains (GVCs) presents a strong case for multilateralism. But this might not be the most important point. No major countries publicly deny the value of a global trade system - the finger always points to someone else when there is a failure of agreement. The United States thought its Trans-Pacific Partnership (TPP) and Trans-Atlantic Trade and Investment Partnership (TTIP) strategies would be a detour on the way to its destination of the top of the mountain.

Two other points are important. The first is the necessity of promoting healthy competition and synergy between regional initiatives, rather than stopping them. The G20 process could be a platform for trade ministers to exchange information and discuss possible approaches for synergies among the TPP, Regional Comprehensive Economic Partnership (RCEP), TTIP and others, in addition to renewing their commitment towards revitalising (or ‘rescuing’, in the words of Cheng Deming, the former Chinese Minister of Commerce) the WTO. One reassuring factor is that, historically, interactions between RTAs and the WTO have been positive in the end.

Point two is the most fundamental: to think beyond trade for trade, which means getting rid of, or reducing, domestic political obstacles and other bottlenecks (such as the shortage of infrastructure) that prevent greater trade flows. Trade liberalisation is very political, and often needs a bottom-up and beyond-trade agenda. President Xi Jinping proposed, in the 2013
APEC Leaders’ summit, to better integrate social policy with economic policy. Like the Russian presidency initiated Joint Finance and Labour Ministers Meeting, Trade Ministers could also consider inviting Labour Ministers and others to join in, in the hope of achieving more comprehensive and reliable solutions.

**Contributing to the post-2015 development agenda**

Development is not only a matter for both the economy and society, but it also encompasses notions of security. However, the post-2015 development agenda is fundamentally about bridging two divides: one between growth and environment (in other words, capital and sustainability), and the other is between traditional and emerging powers (or the so-called South–South cooperation and South–North cooperation). Considering that it involves the highest leaders of the most important economies, the G20 should assist in coordinating and narrowing the gaps, but not repeat what the UN is doing in terms of the preparation of documents.

For the first gap, the post-2015 goal is to integrate three processes: UN-development, UN-environment and the United Nations Framework Convention on Climate Change (UNFCCC). The real challenge is to coordinate the UN process and the UNFCCC process. Traditional development financing is facing a challenge from the tremendous expectations that have grown around climate financing demands. The major economies within the G20 should stop separating these two tracks, and commence work on coordinating the two processes more effectively. Fundamentally, this goes back to the earlier discussion about widening the sources of financing for investment.

Regarding the second gap, the G20 is a perfect platform for emerging economies to hold dialogues with traditional donors at a ministerial level about basic issues such as how to deliver official development assistance (ODA) more effectively, in a cooperative way, and what the indicators should be. The OECD used to be the dominant player in setting rules for ODA, however the emerging economies within the G20 are reluctant to endorse a body of which they are not a member.

**Notes**

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