

The G20: A New Experiment in Global Governance

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(Paper contributed to festschrift for Prof. Lord Meghnad Desai)

It is a pleasure to contribute to this Festschrift for my good friend Meghnad Desai. I have known Meghnad for many years in a staggering variety of avatars: as a one-time Marxist economist, a mainstream economist/econometrician at LSE, a Labour Party activist, a Labour Member of the House of Lords (*I was his guest in the gallery when he spoke in support of Tony Blair's decision to send British troops into Iraq*), a keen and surprisingly good cook, an insightful observer of the Indian political scene, a regular columnist in one of India's leading newspapers, a biographer of one of the best-loved Bollywood icons of yesteryear, most recently a late-blossoming novelist, and above all a wonderful raconteur and bon vivant!

Meghnad's multifaceted personality allows the widest possible latitude in choosing a subject for an essay in his honour. As he is quintessentially a global citizen, I thought it would be both appropriate and topical to write on the G20 and its role in global governance. Section I presents an assessment of the performance of the G20 in the first two years when it was dominantly concerned with managing the global crisis. Section II presents an assessment of the challenges facing the G20 in undertaking a more holistic reform of the international monetary system. Section III comments briefly on other tasks before the G20 and Section IV comments on the issue of the legitimacy of the G20 as a mechanism for improving global governance.

I. The First Two Years: Managing the Crisis

The decision to convene the first meeting of what later became the G20 at the summit level¹, was taken shortly after the collapse of Lehman Brothers transformed what, until then, had been viewed as a serious but limited problem affecting the housing loan market in the United States into a full-blown financial crisis. Both Prime Minister Brown of the United Kingdom and President Sarkozy of France called for a second Bretton Woods-type Conference to examine the functioning of the system as a whole.

The severity and breadth of the crisis dictated that consultations would have to go beyond the G8 and involve a larger group of emerging market economies, which

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¹ The G20 was originally established in 1999 as a forum of finance ministers and central bank governors of 19 important advanced and emerging market economies plus the EU to discuss issues related to the functioning of the international monetary and financial system. It has met annually since then. The first meeting of the Heads of Government of these 20 countries was held in November 2008 in Washington DC.

now accounted for a substantial share of global output and trade, and an even larger share in global growth. President George Bush therefore invited the leaders of the Group of 20 to meet in Washington DC in November 2008, to discuss measures to deal with the crisis. The leaders met again on two occasions in 2009, first in London and then in Pittsburgh, and twice again in 2010, first in Toronto and then in Seoul. To examine whether these meetings were successful in handling the crisis, we first consider the end results, and then the nature of the specific actions taken.

The position as far as end results is concerned is summarized in Table 1, which shows the outcomes in terms of growth rates of GDP for the world and also for the advanced countries and emerging market and developing countries separately. Projections made for 2009 and 2010 by the International Monetary Fund (IMF) in its successive World Economic Outlook (WEO) updates are shown, along with the actual outcomes.

Table 1
Growth Rates of GDP Projected and Actual
(Percentage growth over previous year)

	2007	2008	2009		2010		2011	
			WEO	WEO	Actual	WEO	Actual	<u>Projection</u>
			<u>(Nov.08)</u>	<u>(April 09)</u>	<u>Outcome</u>	<u>(April 09)</u>	<u>Outcome</u>	
1) World Output	5.4	2.9	2.2	-1.4	-0.5	2.5	5.0	4.4
2) Advanced Countries	2.7	0.2	-0.3	3.8	-3.4	0.6	3.0	2.4
3) Emerging Market & Developing Economies	8.8	6.1	5.1	1.5	2.7	4.7	7.3	6.5

After growing at 5.4 per cent in 2007, world output growth slowed down to 2.9 per cent in 2008. The advanced economies were initially projected to contract by 0.3 per cent in 2009, while the developing countries were projected to grow at 5.1 per cent but these projections were subsequently revised sharply downwards in the WEO update for April 2009, which showed the world contracting by 1.4 percent and advanced countries contracting by 3.8 per cent, while the developing countries grew by only 1.5 percent.

The rapid downgrading of growth prospects in 2009 led to a substantial policy response described later in this section. As it turned out, the world performed better in 2009 than was initially feared. The contraction in 2009 for the world as a whole was only around 0.5 per cent, instead of 1.4 per cent projected earlier. The advanced countries contracted by 3.4 per cent instead of 3.8 per cent projected earlier and the emerging economies did much better, expanding by 2.7 per cent instead of 1.5 per cent predicted earlier.

The recovery in 2010 was stronger than originally expected. The WEO for April 2009 initially estimated growth in world output in 2010 at 2.5 per cent but world output actually grew at 5.0 per cent in 2010. The advanced countries grew at 3.0

percent and the developing countries at 7.3 per cent, instead of the 0.6 per cent and 4.7 per cent respectively, projected in April 2009.

Given the scale of the shock, which at one time seemed reminiscent of the Great Depression, the fact that the world economy recovered smartly after only one year of negative growth has been remarkable. The recovery has not been without problems: unemployment has remained stubbornly high in industrialized countries and inflationary pressures have surfaced in emerging market countries. The sustainability of the recovery is also clouded by the sharp increase in public sector deficits and debts in most of the advanced economies, including in particular, the United States, Japan and many of the European countries. The fragility of the Eurozone at the time of writing (mid 2011) added a new source of concern. These are worrying problems but they do not negate the fact that the worst-case outcome of a prolonged depression following the 2008 crisis was avoided. Whether this is because of the corrective policies followed as a result of the G20 consultations, or whether the earlier projections were simply over pessimistic, is difficult to establish with certainty. However, the benefit of doubt should surely go to the G20.

a) Understanding the nature of the crisis

Correct diagnosis is the first step in defining correct solutions and one of the stated objectives of the first meeting in Washington in November 2008 was to achieve a better understanding of what caused the crisis. The G20 consultations did well in this area because they helped move the public debate away from somewhat simplified perceptions of the causes of the crisis, towards a more nuanced understanding, which helped evolve a consensus on how to move forward.

Initially, there was a tendency to over simplify by tracing the crisis solely to the excessively large surpluses in some countries, notably China and the oil exporting countries, and the recycling of these surpluses back to the U.S. in the form of large reserve holdings of US dollar securities. The build up of reserves was seen as reflecting a conscious decision not to allow the currency to appreciate, thus interfering with the mechanism for adjustment. The inflows resulting from reserve accumulation were seen as causing excess liquidity in the United States, which drove down long-term interest rates, promoting risky forms of financial innovation and reckless lending in search of higher yield, which in turn produced financial fragility.

On this view, much of the blame for the crisis lay with the relentless drive for exports as a source of growth, facilitated by an exchange rate that was deliberately undervalued. This in turn suggested that corrective steps should focus on the need to introduce “discipline” on surplus countries, including pressure for appreciation of the currency. Not surprisingly, this view was strongly opposed by the surplus countries, who typically argued that the other side of large surpluses was large deficits, which reflected macro-economic imbalances that should have been tackled internally.

After much discussion among Finance Deputies and Ministers, the G20 Summit endorsed a more balanced assessment, recognizing the multiple causes of the crisis. Unsustainable global imbalances and the absence of self-correcting

mechanisms had plagued the global economy for several years, and certainly represented one part of the problem. However, there were several other factors that were also responsible for the financial vulnerability that led to the crisis. These were: (i) the regulatory philosophy of financial regulators in some of the major industrialized countries, which placed too much faith in the efficiency of financial markets, (ii) the unwillingness to tighten money supply despite asset price bubbles created by excess liquidity, (iii) inadequate understanding of the risk associated with several of the new financial products created by financial innovation, (iv) toleration of excessive leverage in financial institutions, especially in the shadow banking sector, which contributed to system vulnerability, (v) inadequate capital buffers and a pro-cyclical bias built into Basle II mark-to-market practices, (vi) unrealistically low assessment of risk for securitized assets based on poor credit rating practices and (vii) compensation practices in the financial sector which greatly encouraged excessive risk taking.

The relative role of all these factors was not spelt out precisely in the Washington communiqué, but they were sufficiently acknowledged to avoid placing blame on only some elements. This set the stage for evolving a common position on what might be an appropriate architecture for financial sector reform and also lay the basis for exploring mechanisms of macro-economic coordination to overcome global imbalances.

b) *Policies to counter recession*

Issues related to reforming the financial regulatory system occupied the headlines in the immediate aftermath of the crisis but these were essentially relevant over a longer time horizon. The financial sector was so shell-shocked in the short term that there was little danger of excessive risk-taking and the immediate problem was how to inject liquidity and overcome an irrational unwillingness on the part of banks to lend. The more urgent task was to counter the downturn in the real economy.

There was considerable resistance in many quarters to adopting expansionary Keynesian policies. Part of the problem was the initial tendency in Europe to see the crisis as a problem of the Anglo Saxon banking system, whereas the fact was that global financial interconnectivity had made large parts of the European banking also vulnerable, a weakness that would exert a contractionary effect on the real economy.

Despite differences in perception, the G20 consultation in London in June 2009 did produce a consensus in which most of the industrialized countries resorted to varying degrees of fiscal and monetary expansion compared to what was envisaged earlier. This was not the result of any formal agreement on the extent to which fiscal policy would be expansionary, or monetary policy eased, in particular countries. The most that can be said is that the consultation process helped to evolve a consensus that enabled G20 leaders to state that primacy must be given to economic recovery, leaving it to individual countries to choose the extent of fiscal or monetary expansion they would attempt. In other words, the countries acted in concert though they did not actually coordinate.

The commitment to pursue expansionary policies was reiterated at the Pittsburgh Summit in September 2009. The communiqué specifically referred to a determination to avoid any 'premature withdrawal of stimulus' although it was also noted that exit strategies would be prepared to withdraw support in a 'cooperative and coordinated way' when the time is right. The G20 had a difficult balancing act to perform. Both external and internal public sector imbalances in the industrialized countries pointed to the need for fiscal consolidation, but private sector balance sheets had been so damaged by the asset price collapse caused by the crisis that private demand could not be expected to take up the slack and indeed, was expected to have a contractionary effect.

By the time of the Toronto meeting in June 2010, perceptions had changed. A recovery was clearly underway, and although there were worries about a possible "double dip" recession, concern about the consequences of fiscal imprudence had also increased. The Conservative-Liberal coalition which had come to power in the United Kingdom was committed to an earlier exit from fiscal stimulus and this reinforced German views on this issue. The G20 communiqué from Toronto, therefore, signalled a stronger commitment for an earlier exit for countries with serious fiscal challenges. The concerns of those worried about the contractionary effect of an early exit were sought to be addressed by stating that fiscal deficits would be halved by 2013, thus indicating the goal at the end of three years without specifying the annual phasing. It was hoped that this approach would reassure markets about the longer term commitment to restoring fiscal sustainability, while avoiding immediate contraction in demand.

A missing element in the discussion on policies to counter recession was that there was no strong commitment on the part of surplus countries to expand domestic demand to counter demand contraction in deficit industrialized countries. In the absence of such a commitment, the stimulus would have to be continued in deficit countries if the level of economic activity was to be maintained, even if it worsened the public debt balance. This meant that demand was being sustained, but the underlying global imbalances were not being corrected. That correction could only occur if the G20 could achieve the more difficult task of coordinating macro-economic policy across countries, with surplus countries expanding demand while deficit countries contracted.

c) Co-ordinating macro-economic policy

The advantages of coordination of policy have been discussed extensively in the literature. When a single country has an imbalance, and the rest of the world is broadly in balance, it is reasonable to expect that corrective action has to be taken primarily by the country with the imbalance, and coordination with other countries is less important. However, when some countries have unsustainable deficits and others have excessive surpluses, as has been the case for several years, what is needed is symmetric adjustment in which both the deficit and the surplus countries undertake some adjustment. The willingness to accept demand deflation in a deficit country would be greater if there were assurance that demand elsewhere is being increased

simultaneously, mitigating the negative effect on employment. Equally, the willingness to inflate demand in surplus countries should be higher, if fears of overheating are reduced, because of the knowledge that demand elsewhere is being reduced. Coordination can therefore lead to an optimal outcome in such a situation.

IMF surveillance conducted under Article 4, involves surveillance of the policies of each country individually, and is ill suited to achieving coordination of policies across countries. The IMF also undertakes broader assessments of the global economic situation through the World Economic Outlook, the Global Financial Stability Reports, and more recently through the Fiscal Monitor, but these do not involve discussion of individual country policies in the context of what other country policies might be.

The need for multilateral consultations to deal with global imbalances was recognized in the middle of the last decade when the United States current account deficit rose year after year, reaching 6 per cent of GDP in 2005. There was widespread concern that if these large imbalances, affecting the major reserve currency country, were not reduced through some form of soft landing, a much more disruptive hard landing would become inevitable. Departing from past practice, the IMF sought the cooperation of the five entities that account for the bulk of the surpluses and deficits - the United States, the Eurozone, China, Japan and Saudi Arabia - to undertake a multilateral discussion of the actions each might be willing to take to address the problem.

This initiative was not particularly successful. Raghuram Rajan, then Chief Economist of the IMF, reports that to prepare for the international meetings, the Fund engaged in preliminary discussions with each of the five to see if some agreement could be evolved. The outcome, described in Rajan, (2010), is sobering: *“The response from our interlocutors was pretty uniform. Countries agreed that the trade imbalances were a potential source of instability and economic reforms were needed to bring them down before markets took fright. But each country was then quick to point out why it was not responsible for the imbalances and why it would be so much easier for some other country to push the magic button to make them disappear.... When the consultations eventually concluded in 2007, the Fund declared that they had been a success: there had been a free and frank exchange of views, which is bureaucratise for total disagreement.”*

The G20 rightly chose not to be discouraged by this earlier failure and embarked on a bold new initiative to develop a mechanism for policy coordination among the G20 countries through a Mutual Assessment Process (MAP). Unlike the normal IMF surveillance process, in which the IMF is the principal interlocutor, the MAP process is expected to be led by the G20 countries themselves, with the IMF, along with other international organizations, only providing technical assistance.

A two-stage framework for this multilateral process was developed. In the first stage, seven statistical indicators were used to identify countries with large external and internal imbalances. The indicators include three, which relate to the external balance (balance of trade in goods and services, income and transfer balance, and net

external balance) and four, which relate to internal balance (primary budget balance, public debt, private debt, and private savings). These indicators have been used by the IMF in different ways to identify imbalances which appear large. On this basis, seven systemically important G20 countries as having large imbalances, and the policies of these countries will be subjected to special scrutiny in the second stage².

Each G20 country has also been asked to submit its projection of major macro-economic variables based on a common template over a five year horizon. These individual country projections will be analysed by the IMF as part of the MAP to assess what they imply for the global economy. Since the G20 account for about 78 per cent of global output, aggregation of the individual country projections does provide a reasonable basis for scaling up to global GDP, and comparing the aggregate of the country projections with the global projections made by the IMF. It also provides a basis for assessing whether individual country projections are based on assumptions about global outcomes which correspond to the actual global outcome that would result if individual countries proceed as projected. Inconsistency between the global growth assumed in individual country projections, and the global projections resulting from the aggregation of individual projections or from the IMF's global forecasts, can be resolved through interaction. This would give the IMF a basis for assessing what global growth and global imbalances would be if the countries policies proceed on the lines indicated.

In the case of the seven G20 countries selected for second stage scrutiny, the individual country projections will be analysed on the basis of indicative guidelines regarding policy action that might be appropriate to correct the imbalances, taking account of the specific circumstances of each country. From this process, it is expected that the IMF will be able to define an "upside scenario" for the global economy, assuming that the seven systemically important countries follow the policies which can lead to the upside scenario. This upside scenario can then be viewed as the goal which successful policy co-ordination can achieve.

The IMF assessment, along with reports by other international organizations, will be presented to the Framework Working Group (FWG) of G20 finance officials and the FWG will then present a single MAP report to the finance ministers. The FWG's MAP report is expected to reflect the collective view of G20 members, informed by reports produced by the IMF and other international organisations. The MAP report after being considered by the Finance Ministers will be presented to the Cannes Summit in November 2011.

It remains to be seen whether the proposed MAP process will be more successful than the IMF's last attempt at multilateral surveillance in 2007. A key difference is that instead of the IMF conducting the process, it is country driven, with the IMF only providing technical assistance. However, that by itself does not make it any easier. Participating countries are likely to defend their own positions strongly,

² The G20 have not announced the list of countries but the list has been discussed publicly. Angeloni and Pisani-Ferry (2011) report that the list consists of the United States, United Kingdom, France, Germany, Japan, China and India.

but are less likely to take strong positions when differences arise between other countries. The absence of an external arbiter pronouncing on these issues has the advantage of avoiding what may otherwise appear as intrusive intervention by the IMF, but it will also make it difficult to resolve differences. The danger in such situations is that difficult issues will be obfuscated through creative drafting rather than meaningfully resolved.

The technical complexity of each step of the exercise should also not be underestimated. It is very difficult to determine objectively when an imbalance in a particular country is unsustainable, especially if the assessment is meant to be forward-looking rather than simply a statistical exercise identifying outliers based on past trends. It is even more difficult to determine what precise mix of policies is appropriate to address the imbalance in a particular country. Such assessments can only be made on the basis of some implicit assumption about the structure of the economy, which determines its response to policy intervention, and the time lags involved. There is enormous room for honest differences of opinion on each of these issues. The margin of error involved in estimating the extent of change needed in particular policy instruments to achieve a given outcome is so large that judgement rather than technical analysis has to play the dominant role. Besides, since the policies of one systemically important country will affect other countries, it will always be possible to argue - as countries did on the last occasion - that the correction of an imbalance in any one country depends more on changing the policies of other countries.

The IMF routinely makes projections about the world economy and also makes judgements about broad directions of policy based on various economic models of the world economy and its regional components. These projections can also be questioned on the same basis, but countries have much less incentive to question projections about the world economy, and even recommendations on broad policy directions for groups of countries or regions. They will subject country specific policy conclusions to much greater scrutiny.

Despite these difficulties, it can be argued that the value of the process is much more in the process itself, and the impact that it may have over time in developing a shared approach among participating countries, rather than in the ability to resolve current differences. Coordination of policy among sovereign countries is never easy, and is unlikely to be achieved through collective decision making based on some form of voting to resolve differences. It is more likely to occur because the policy of each country is influenced, gradually if not immediately, by the collective sense of the community of G-20 members. In other words, multilateral surveillance has to be viewed as an exercise in persuasion.

The IMF has an important role in this process, even if it is not the arbiter of outcomes, by providing high quality technical inputs, and also indicating where the case for policy change is compelling and where it is more marginal. However the IMF's ability to ensure that technical issues are not lost sight of is limited by the structuring of the MAP exercise, in which the IMF's input is primarily at the FWG level, after which the FWG prepares the report that goes to the finance ministers and

the summit. There is a case for the G20 establishing a technical advisory group of eminent experts who might be asked to comment on the technical work of the IMF, and also on the consensus emerging from the FWG. The views of these experts should be available in subsequent stages to ensure that difficult issues are suitably highlighted for the Summit rather than papered over. Such a mechanism is particularly necessary since there is no G20 secretariat.

d) *Creating a new architecture for financial regulation*

The need for reform of the financial system was recognized as a priority in the very first meeting in November 2008. Subsequently, there have been several expert reports on the subject, including assessments by regulators within individual countries. Much of what is involved is technical and not what one would expect leaders to pronounce upon. However, the G20 Summits can claim to have imparted a sense of urgency on the need to act, and also endorsed the broad direction of action.

At the first meeting in November 2008, the G20 endorsed the principle that financial markets must remain open, competitive and transparent, but they must be much better regulated to reduce risk-taking behaviour and avoid pro-cyclicality. It was also made clear that better regulation did not mean establishment of a supranational financial regulator which had been talked about. As the November 2008 communiqué put it, “Regulation is first and foremost the responsibility of national regulators who constitute the first line of defence against market instability. However, our financial markets are global in scope, therefore, intensified international cooperation among regulators and strengthening of international standards, where necessary, and their consistent implementation is necessary to protect against adverse cross-border regional and global developments affecting international financial stability.” Those who favour stronger supra-national regulators may not be happy with this decision, but it was the only approach acceptable, including by emerging market countries.

The erstwhile Financial Stability Forum, which had been set up after the East Asian crisis, but which did not include emerging market countries, was broadened to include all G20 countries and renamed the Financial Stability Board (FSB). This was clearly an important act of democratization, increasing ownership by the emerging market countries of action taken by the FSB. The FSB was expected to work with the international standard-setting bodies and encourage them to develop a new architecture for financial regulation.

An important outcome of this effort is the set of new Basle III standards, issued by the Basle Committee on Banking Supervision. The new standards contain many significant improvements such as (i) improved quality and transparency of the capital base, (ii) provisions for capital buffers which can be built up in good times and drawn down in bad, thus reducing pro-cyclicality, (iii) leverage ratios that put a limit on total leverage, and (iv) various measures designed to limit risk, including the use of longer-term data horizons to estimate probabilities of default. The target for full implementation is December 31, 2019 which gives considerable room for national regulators to determine the pace of adherence in a manner that will be least disruptive.

The G20 can legitimately claim that it is because of the commitment expressed at the highest level that Basle III took only two years to complete, whereas Basle II took ten years!

This is not to say that all aspects of financial architecture have been resolved. Some of the most difficult issues in dealing with financial stability have yet to be addressed. Basle III covers banks, but does not directly address potential vulnerability arising from the shadow banking system which is very large compared to the banks in industrialized economies. Problems associated with cross border resolution in banking crises, and also the problems of institutions that are too big to fail, also remain unresolved. The supervision of financial institutions operating in more than one jurisdiction, based on a college of supervisors approach, has also yet to be tested in practice.

These weaknesses notwithstanding, there is no doubt that a start has been made with considerable convergence of thinking among all the major countries. The task of creating a new financial architecture is bound to be an ongoing process and at this stage it is likely to make more progress if taken out of the limelight summits.

e) *Strengthening the International Financial Institutions*

One of the important achievements of the G20 in the first two years is the strengthening of the International Financial Institutions (IFIs) by providing additional financial resources and also improving the voice of developing countries within the institutions. The provision of additional resources was viewed as especially important as it would enable these institutions to help developing and transition countries to cope with a global downturn which was expected to reduce their exports and possibility also trigger a reversal of capital flows.

IMF quotas were doubled to about SDR 477 billion, a much bolder step than was earlier thought likely. This was accompanied by an interim increase in the size of the New Arrangements to Borrow, pending the quota increases becoming effective. A new issue of Special Drawing Rights (SDRs) amounting to SDR 270 billion was also agreed, providing unconditional liquidity to many countries in need. Two new IMF facilities were introduced which provided much greater flexibility to borrowers. One of these is the Flexible Credit Line, for countries with very strong fundamentals and a track record of implementation. The facility provides large resources upfront with no policy conditionality. The other new facility is the Precautionary Credit Line, which is also meant for countries with strong fundamentals, but which have some moderate vulnerabilities. This facility therefore entails some conditionality, aimed at addressing these vulnerabilities, and disbursement is trenched.

Long-standing demands for increased representation from the developing countries have also produced some response. Quota shares have been adjusted by shifting 6 per cent of the total share to the 'dynamic emerging markets and developing countries' and another 6 per cent shift from "overrepresented" to "underrepresented" countries. The net effect has been to reduce the quota share of the older European members and the United States though still leaving the United States with enough

voting share to have an effective veto on major issues, which require an 85 per cent vote.

The multilateral international development banks are an important part of the international financial system from the perspective of developing countries. They are less important than they used to be for the emerging market group within the developing countries, but they remain very important for smaller developing countries that lack access to capital markets. The World Bank's capital was increased by 50 per cent the Asian Development Bank by 100 per cent and the Inter American Development Bank capital by 70 per cent. Quota shares of the developing countries in the World Bank have also been increased as a consequence of the increase in the IMF.

It can be argued that these decisions had been under consideration for some time and could have been taken in the normal course. However, anyone familiar with the resistance and inertia that prevented movement earlier, would agree that the direct engagement of the G20 leaders at the summit level, prompted no doubt by the crisis and the need to respond to developing country demands, helped resolve what otherwise might have taken much longer, and indeed may not have come to as satisfactory an outcome.

f) *A moratorium on protectionism*

Finally, the moratorium on additional protectionist measures, which was a part of the commitment of the G20 repeated in successive communiqués, deserves to be counted as an important achievement. It can be argued that these commitments were not strictly observed, since many G20 countries introduced some measures that could be described as increasing the level of domestic protection. However, all these actions were strictly monitored by the WTO, which reported back to G20 leaders at each summit. The gist of the WTO assessment thus far has been that while almost all countries introduced some measures, the overall impact of the measures was small.

The G20 did therefore live upto the promise of avoiding any serious risk of a relapse into protectionism which would have been devastating for the world economy. In this respect the world was spared the protectionist-type reaction witnessed at the time of the Great Depression, when the Smoot Hawley Act was passed in the United States.

II. Reforming of the International Monetary System

In addition to crisis management, a task which has once again moved to the front burner because of the Eurozone crisis, the G20 must also turn to the broader issue of whether the present International Monetary System (IMS) is capable of meeting the needs of the global economy or whether some basic structural redesign is needed. Some important steps have already been taken, but these amount to fixing the system where it was obviously broken. A holistic review of the system as a whole is needed and this is expected to be part of the agenda at the Cannes Summit in November 2011.

a) *Weaknesses in the present system*

A central issue that must be addressed at the outset is whether the present system of exchange rates between major currencies should continue or whether there is a change that is feasible and desirable. This paper proceeds on the assumption that no practical alternative exists to the present system of floating exchange rates between the currencies of major countries, (treating the Eurozone as one unit for this purpose) with other countries adopting a variety of exchange rate arrangements ranging from free floating to various types of managed floats, soft pegs, or even hard pegs if preferred. The main weaknesses of the system, which any restructuring of the IMS must address, are the following: (i) excessive volatility in exchange rates, combined with persistent misalignment reflecting the absence of automatic adjustment mechanisms (ii) excessive dependence on the US dollar as the reserve currency, which also reduces pressures on the United States to adjust, (iii) excessive volatility of capital flows reflecting high levels of capital mobility with not enough underlying stability in the world economy and (iv) insufficient assurance of availability of international liquidity, especially in crisis situations. These weaknesses obviously feed on each other. Persistent misalignment of exchange rates can lead to large reserve holdings in dollar assets and this in turn raises the threat of currency instability following a possible portfolio shift.

No grand design for reform has emerged thus far although considerable useful work has been done on this issue e.g. the Report of the Palais Royale Initiative (2011) and a report to the European Commission by Angeloni et al. (2011).

b) *Reducing volatility and mismanagement*

There can be no doubt that the global real economy would benefit from lower volatility of exchange rates and smoother adjustment when exchange rates are misaligned. In a world of floating exchange rates, this is best achieved by more effective policy coordination across countries to avoid the kind of imbalances which can otherwise create destabilizing exchange rate movements. The G20 MAP initiative is designed precisely to address this issue. If it does make some progress, the G20 can legitimately claim to have created one of the major building blocks for ensuring a well functioning global economy in today's world.

The problems of achieving coordination are formidable. Deleveraging in the industrial world will mean weak private demand, while existing and projected public sector imbalances in these countries limit the scope for fiscal policy. Monetary easing in the industrialized countries has also reached the limit of its possibilities, with low interest rates threatening another asset price bubble, and also potentially large spillover effects on emerging market countries through volatile capital flows. East Asia has depended heavily on exports and needs to shift rapidly to a domestic demand led strategy with greater exchange rate flexibility³. However, perceptions vary on the

³ There is recognition of the need for such a shift, and China's Twelfth Five Year Plan explicitly talks of a consumption-led strategy with a lower growth rate.

pace at which the shift can occur. Germany too has relied heavily on export demand and presents similar problems. It is sometimes argued that the German surplus is offset by deficits in other Eurozone countries, and as long as the Eurozone as a currency area, is in balance, the German surplus should not matter. However, the deficits in some of the Eurozone countries are not sustainable unless there are assured fiscal transfers bailing them out. If this is not feasible, and demand in these countries has to be contained, then global rebalancing will require an increase in German domestic demand. It remains to be seen how effectively the MAP can resolve these problems.

c) *Dominance of the dollar*

The dominance of the US dollar, relative to the other reserve currencies has long been a source of asymmetry in the system, giving the United States the “exorbitant privilege” of being able to finance its deficit by issuing claims denominated in its own currency. Since this dominance is not due to any international agreement or compulsion, but is solely the result of market choices, it can be argued that it is a legacy phenomenon. On this view, the importance of the US dollar will decline gradually. It will, of course, remain one of the major reserve currencies, and indeed the most important for quite some time, but a better balance with other currencies will emerge on its own.

However, the massive accumulation of US dollar assets in reserves increases the risks of exchange rate volatility if reserve holders seek to diversify their holdings. One way of solving this problem is to allow dollar reserves to be converted into SDR reserves, reducing the danger of portfolio switches away from the dollar. The mechanism envisaged is one in which holders of dollar reserves can convert their excess reserves into SDR denominated reserves held in a special account in the IMF. These SDR denominated assets could be used by holders to settle claims with other central banks, or converted into desired currencies by the IMF using the dollar assets originally deposited with it.

Countries could achieve the same objective by diversifying their reserve holdings to reflect the same proportion of different currencies as the weight of the component currencies in the SDR, but this process would involve a net offloading of dollars in currency markets with consequent exchange rate effects. Freezing the dollar holdings in a special account in the IMF forestalls such pressures in currency markets, but it entails an exchange risk for the special account if the dollar depreciates over time. The need for a substitution account of this type was discussed in the late 1970s, but it never took off because the issue of who would bear the exchange risk could not be resolved.⁴

⁴ The extent of exchange loss would depend on the net effect of the change in exchange rates plus the differential between the interest earned on dollar securities and the interest paid on the SDR holdings.

d) *Role of the SDR*

The case for giving the SDR a larger role in the IMS has been a recurring theme in the literature on international monetary reform. It has been raised again recently by Zhou Xiaochuan, in a much quoted article 'Reform of the "International Monetary System"' which suggests that the SDR should progressively replace the dollar in global reserves and should also become a multilaterally controlled mechanism to increase global liquidity. There are several different issues that arise in this context that need to be addressed.

It is sometimes asserted that increased reliance on the SDR will help reduce volatility in exchange rates between the major currencies. Since the SDR is itself a basket of currencies, and not a separate currency, it is not immediately obvious how it can actually add to stability of other currencies except by preventing large dollar holdings from being offloaded in the market. Fluctuations in the exchange rates of currencies composing the basket result from the operation of currency markets, which in turn are driven by changes in the underlying economic fundamentals of the corresponding economies, or expectations about these fundamentals. Efforts to reduce exchange rate fluctuations must therefore focus on measures which will dampen sudden changes in those fundamentals, or manage the changes better. This takes us back to co-ordination mechanisms such as the MAP, which have to be used to generate more orderly adjustment processes. Conversion of dollars into SDRs in a special account would reduce the risk of volatility, but this is possible only if the exchange risk problem can be resolved.

The case for enlarging the role of the SDR is sometimes made in terms of the need for regular new allocations of SDRs. Regular allocations would add a steady dose of liquidity, based on multilaterally determined rules which could build in an element of counter-cyclicality. Since the SDR is not "outside money" but only a line of credit, it should not have significant inflationary impact. To the extent that the availability of unconditional liquidity reduces the need for building up owned reserves, it can be said to avoid behaviour that is otherwise contractionary. The quantitative impact of modest but regular new allocations on inflation will be small. Even after the recent increase in SDR allocations, the total outstanding stock of SDRs is only 4 per cent of total foreign currency reserves.

The fact that the resulting liquidity would be distributed to countries in proportion to their share in Fund quotas has been criticised as a departure from purely market-based criteria for providing credit, but this criticism is overdone. Extending some additional liquidity to weaker countries can be justified on equity grounds, especially since the poorer countries suffer so many other disadvantages.⁵ What regular SDR allocations will do is increase the cushion of confidence that countries have, while also creating considerable potential liquidity which would be useful in abnormal times, when private capital markets freeze.

⁵ It should be noted that the rule of proportionality to quotas ensure that the bulk of the additional liquidity provided goes to countries that will not use it. It is instructive that 90 per cent of the new SDR allocation made in the post crisis period remains unused.

If we want to increase the role of the SDR in global reserve holdings, it makes sense to increase the usability of the SDR in non-official transactions. Several proposals for doing so have been advanced, and could be implemented in a gradual manner. These include the issue of SDR denominated bonds by the IMF and also the promotion of SDR denominated pricing of major commodities. Wider use of the SDR as a unit of account in invoicing of world trade will certainly dampen the effect of fluctuations among the major currencies on prices denominated in SDRs. However since the prices that affects the real economy are the domestic prices in individual countries, based on the currencies in use, a mere dampening of SDR denominated prices is only an averaging phenomenon.

Finally, if the SDR is to continue as an important part of the international monetary architecture, it makes sense to establish transparent rules whereby currencies of countries which meet certain criteria of economic size and currency convertibility can be included in the basket. The Renmimbi is the obvious currency which could be added to the SDR basket, though it would be necessary for it to have much greater flexibility for use in capital transactions, which in turn implies much higher exchange rate flexibility. The issue of exchange rate flexibility is particularly relevant since otherwise adding the Renmimbi into the SDR basket only amounts to increasing the weight of the US dollar. Logically, there should be periodic review of the composition of the SDR basket providing for both entry and exit of currencies. Looking further ahead, say over the next twenty years, the role of both the yen and sterling are likely to decline. A case can also be made for well-defined, rule-based surveillance, by the IMF, of the currency regime of countries whose currencies are in the SDR basket.

e) *Managing capital flows*

It is generally agreed that long term capital flows, including especially Foreign Direct Investment (FDI), can improve global allocation of resources and bring about faster growth of developing countries. However, the volatility of capital flows, “with sudden stops” and surges, poses serious risks. This is the main factor explaining the “fear of floating” which characterizes many developing countries, and explains their adoption of exchange rate regimes which allow for flexibility, but retain the option of intervening including by the introduction of capital controls. Developing countries therefore need a framework for regulation of capital flows, which enables them to reap the benefits of global financial integration, while limiting the risk involved.

A sound financial sector is clearly one element of such a framework. One of the lessons of the East Asian crisis of 1997 was that weak financial institutions intermediating foreign flows can expose countries to serious currency mismatch risks, which can generate extreme financial vulnerability, which in turn can provoke a crisis. Most Asian countries have already taken significant steps to deal with this problem and the ongoing global efforts to strengthen the financial system will help further in this respect. Building owned reserves is another mechanism to insulate the economy from volatile capital flows and many emerging economies have taken steps in this

direction. The possibility of using capital controls is another mechanism for managing capital flows.

The use of capital controls was a contentious issue in the 1990s, when the conventional wisdom in industrialized countries held that developing countries should liberalize the capital account. There were influential voices arguing against this position - notably Bhagwati (1998) and Williamson (1991) - but the general thrust of opinion, especially in the United States, strongly favoured capital account liberalization. The Articles of Agreement of the IMF do not give it a mandate to oversee the capital account - a hangover from the days when the Fund was created, when the capital account was closed everywhere except the United States. In the second half of the 1990s, the IMF tried to get support for an Amendment of the Articles that would give it a mandate to cover capital account transactions. The effort was strongly resisted at the time by developing countries because it was feared that Fund conditionality would be used to coerce countries to liberalize the capital account.⁶

The intellectual climate today has changed dramatically with virtually universal acceptance that developing countries need to retain some instruments for control over capital flows. The question which arises is whether we should continue with the present arrangements, in which there is no restraint, whatsoever on the controls a country may impose, or whether there should be some agreed international discipline on the action that governments might take to control capital flows, and the surveillance to which this should be subjected. The case for having some discipline is simply that if interconnections on account of trade are regulated by international agreements, then interconnection by way of financial flows should also be subject to some agreed discipline. Of course, trade is different from finance and exact parallels are potentially misleading. However, this should not lead to an automatic rejection of the idea, especially if it is made clear from the outset that the discipline proposed for controls over capital flows should not be designed to push developing countries to acceptance of greater openness.

The issue that needs to be considered is whether we should move to a system where Governments have the choice of deciding the levels of openness to capital flows they choose, but having done so, agree to a discipline on what controls can be introduced beyond that level, and in what circumstances, and also for what period. The objective is only to introduce predictability about what measures can be introduced purely at the discretion of the Government, and what will require some form of international surveillance. A proposal along these lines was outlined in Ahluwalia (2000).

⁶ The timing was particularly unfortunate since the proposal came up in the meeting of the Interim Committee in Hong Kong in 1997, just as the East Asian crisis was breaking out. The move failed, and the initiative was shelved.

f) *Access to multilateral financing*

The recent crisis has clearly demonstrated that the global system needs the IMF as a credible lender of last resort and not just for the developing economies, and transition economies as was once thought. The crises in Greece, Ireland, and Portugal have demonstrated that the IMF may have to be brought into play even for weaker industrialized countries. Some important steps have been taken to strengthen the IMF, but it can be argued that what has been done is an ad hoc response, and not a systemic redesign of the architecture enabling the IMF to play the role it may have to play in future crises. The unprecedented monetary easing resorted to by the US Federal Reserve shows how, in extreme situations, it may become necessary to create additional liquidity on a massive scale.

This raises the issue of whether the IMF should be empowered, based on suitably weighted voting, to create SDRs which it could allocate to itself to use in the event of a crisis. This would take us part of the way to Keynes' original suggestion of creating an International Clearing Union which could issue a new currency to be called Bancor. The SDRs so created could be extinguished when the emergency is over, so that the Fund does not continue to enjoy more liquidity when it is not needed. Suggestions along these lines have been made on several occasions e.g. Ahluwalia (2000) but have not been accepted. There is no reason why the Fund should not be empowered in this way to create liquidity. If the IMF's governance structure is judged to be adequate, the creation of liquidity would be subject to appropriate oversight. If the governance structure is not adequate, it should be suitably modified. This would be a major structural reform, going beyond a mere "fix what is broken" approach.

g) *Increased voice of developing countries in the IMF*

As part of the reform of the system, it is necessary to accelerate the process of giving greater voice to the emerging markets and developing countries in the IMF. The new quotas approved in 2010, which will become effective after ratification, have made some difference. As shown in Table 2, the combined voting share of the four European members of the G20 (i.e. Germany, United Kingdom, France and Italy) will decline marginally from 17.5 per cent to 16.37 per cent and the share of the eight emerging market countries will increase from 12.42 per cent to 15.91 per cent. Even so, the voting share of these countries will be much lower than their share of world GDP, which is 28.34 per cent on the basis of GDP in PPP (purchasing power parity) terms and 20.21 per cent on the basis of market exchange rates.

The next quota review is scheduled to begin in 2013 and be completed by 2014. With more rapid growth projected in the emerging market countries, we can expect a further shift in quota and voting share in their favour. There is a case for accelerating this process by abandoning the existing quota formula, which gives too much weight to foreign trade and reserves. These variables have no particular rationale either as indicators of the need to borrow, or of the ability to contribute. In a world of capital mobility, borrowing needs will be largely unrelated to the size of foreign trade or the current account deficit, and this has been recognized by effectively delinking borrowing limits for individual countries. We should move to a

new formula that uses some combination of GDP at PPP and at market exchange rates, as the base for determining quota contribution and therefore voting rights. Countries that do not wish to contribute on this basis can be allowed to withhold contribution at the cost of lower voting rights, and perhaps also some limitations on access.

Table 2
Distribution of GDP and Voting Share Among the G-20

1. <u>Industrialized Countries</u>	<u>GDP Share</u>		<u>Voting Share</u>	
	<u>PPP</u>	<u>Market Exchange Rate</u>	<u>Present Position</u>	<u>After 2010 Change</u>
EU	20.43	25.88		
USA	19.74	23.30	16.727	16.479
Japan	5.80	8.68	6.225	6.138
Germany	3.96	5.27	5.803	5.308
Russia	2.99	2.33	2.386	2.587
UK	2.93	3.57	4.286	4.024
France	2.89	4.11	4.286	4.024
Italy	2.39	3.27	3.154	3.016
Korea	1.96	1.60	1.364	1.731
Canada	1.79	2.50	2.554	2.214
Australia	<u>1.19</u>	<u>1.96</u>	<u>1.312</u>	<u>1.332</u>
Sub-Total	66.07	82.47	48.097	46.853
2. <u>Oil Exporter</u>				
Saudi Arabia	0.84	0.71	2.799	2.010
3. <u>Emerging Market</u>				
China	13.58	9.34	3.806	6.071
India	5.47	2.44	2.337	2.629
Brazil	2.92	3.32	1.714	2.218
Mexico	2.11	1.65	1.467	1.796
Indonesia	1.39	1.12	0.854	0.951
Turkey	1.29	1.18	0.607	0.953
Argentina	0.87	0.59	0.869	0.661
South Africa	0.71	0.57	0.770	0.634
Sub-Total	<u>28.34</u>	<u>20.21</u>	<u>12.424</u>	<u>15.913</u>

III. Other Tasks Before the G20

The mandate of the G20 covers not only international monetary and financial issues but also other international economic issues. Several of these are already on the agenda and some present especially difficult problems.

a) Completion of Doha Round

One of the most important issues which is on the agenda of the G20 is the need to ensure successful completion of the Doha Development Round. The G20 have

recognised the importance of this item in the global economic agenda by consistently calling for an early conclusion of the Round. Unfortunately, there has been very little progress towards this objective. Trade Ministers have met frequently in Geneva, but the negotiations seem to have reached an impasse. Given the importance of open trade for the growth prospects of the developing countries, it can be argued that the G20 should take on the responsibility of breaking the deadlock to deliver on what has been promised to the developing countries.

The central problem is that some of the industrialized countries have decided that what had emerged thus far in the negotiations - and was in that sense 'on the table' - is simply not good enough and that 'greater ambition' is therefore needed. In practical terms, this means re-opening issues which most participants thought were settled earlier at Hong Kong. Since all such decisions are part of a negotiating process, many participants feel that whatever was agreed was part of a quid pro quo, and re-opening anything involves re-opening everything. This of course would be equivalent to declaring the Round dead, and starting afresh.

The Doha Development Round is the first round of multilateral trade negotiations to have been explicitly described as a development round. Failure to conclude the round will be viewed as a major set back for global governance especially as the Round was meant to deliver disproportionate benefits to the developing countries. In the circumstances, the G20, as the principal forum for discussing international economic issues, will be expected to give a political push to the stalled talks. In some ways, the very usefulness of establishing the G20 as the principal forum of the major industrialized and emerging market countries, to discuss international economic issues, stems from the assumption that it can take up issues that are otherwise blocked in the normal ministerial forum, and bring them for resolution at the highest political level. It remains to be seen whether, by the time of the Cannes Summit, the G20 can take some new initiative in this area.

b) *Climate change negotiations*

A similar test could arise for the G20 in terms of their ability to resolve what look like insuperable barriers to making significant progress on the Climate Change Negotiations. A detailed review of the state of the climate change negotiations is beyond the scope of this paper, but the issues are similar to those in the trade talks. There is an established international forum where this issue is being discussed, but the negotiations in that forum are making very little progress.

There have been some positive developments. The Copenhagen Accord appeared to produce a broad framework of agreement among many participants, which could be developed further. There is also growing agreement on the need to cooperate in some well-defined areas taken in isolation. These are welcome developments and there is merit in being realistic and encouraging progress wherever it is possible. But sooner or later, the world will have to face the fact that a credible deal on climate change will not be possible unless much faster progress is made on how to share the burden involved.

Arguably, the last two years have been the worst years to look for such agreement. Most countries have been pre-occupied with their own domestic problems which include fiscal stress. Hopefully, after the world has got back to economic normalcy, there will be greater willingness to re-engage substantively. Nevertheless, it will be a huge challenge to orchestrate cooperative action on the scale needed and to bear the costs involved. The G20 will certainly be judged by what it contributes to overcome obstacles in this area.

c) *Other issues*

There are several other items on the G20 agenda including unemployment and social security, agriculture and food security, energy security and energy subsidies, transparency in commodity markets, action against corruption etc. The Seoul Summit added development to this already extended agenda. These are important areas in which countries should engage in dialogue to develop commonality of views. But they do not pose any difficult issues for decision in the near future and are therefore not likely to be the basis for judging the usefulness of the G20.

IV. The Legitimacy of the G20

Any assessment of the role of the G20 in global governance has to address the legitimacy issue: can a self selected group of countries ever have international legitimacy? The short answer is that it cannot. However, the real value of the G20 as an international forum is not because it is a legitimized forum for international negotiations, but rather as a more representative replacement for the G8, as the principal forum for discussion of international economic issues.

The need for a broader forum was long evident. The old arrangement, in which the industrialized countries operated as an exclusive club, effectively taking key decisions within the G7/8, and having them ratified later in the relevant international forum, was no longer workable. The steadily rising weight of emerging market economies required that these countries had to be included in consultations on international issues for any meaningful results to be obtained. The G8 Summit in Gleneagles in 2005 acknowledged this reality by inviting five emerging market countries - China, India, South Africa, Brazil and Mexico - to participate, albeit only as invitees for some sessions. This practice was continued in subsequent summits. However, the ambiguous status of the new invitees in this arrangement was a source of discomfort. Celso Amorin, Foreign Minister of Brazil gently satirized the arrangement as the developing countries “being invited to join for coffee”!

Some expansion of the G7/8 was, therefore, inevitable. It could have occurred by adding some more countries to the G8 plus 5. In the event, it occurred because President George Bush decided to convene a summit of the countries which were already members of the G20 at the level of finance ministers. The creation of that group has an interesting history. The decision to set up a group of finance ministers to discuss international monetary and financial issues was taken at the Asia-Pacific Economic Cooperation (APEC) Summit meeting in Vancouver in 1997, immediately after the outbreak of the East Asian crisis. The United States then invited 22 Finance

Ministers to meet in Washington in 1998 at the Willard Hotel (which led to the group being called the Willard Group of 22). The membership expanded to 33, at the next meeting of the group in 1999. However, recognizing the unwieldiness of meetings with 33 countries, the G8, at the Berlin Summit in 1999, decided to establish a permanent Group of 20 finance ministers and central bank governors that would meet regularly to discuss issues related to the international monetary and financial system.

The country composition of the Group of 20 established in 1999 determined the country composition of the G20 Summit. It included all the important industrialized countries, and also the major emerging market countries. Together, the group accounts for 78 per cent of global GDP. However, it leaves out some emerging market countries which have a larger weight than some that are included. Clearly, regional balance considerations played a role in the selection of countries in 1999. There was also no representation for small countries.

Recognizing the limitations of this grouping, the G20 leaders have attempted to broaden participation by a formula which involves five additional invitees. Spain which was not part of the G20 as originally constituted has been made a permanent invitee, in acknowledgement of the size of its GDP. In addition, the head of one of the two African regional organizations will be invited as also a representative of the Association of Southeast Asian Nations (ASEAN). The host of the G20 Summit will have the discretion to invite two other countries. The G20 are also actively pursuing policies of outreach to engage CSOs, business leaders, and other countries, on items on the summit agenda.

None of this can confer formal legitimacy to the group. But it does help to create an environment in which the activities of the G20 are more transparent, and open to comment by others who are not members. In the end, the effectiveness of the group will depend on the fact that the countries included in the group account for almost 80 per cent of global GDP. If consensus is reached in this group, it should be possible to translate it into a global consensus. The translation is easy in the case of international financial and monetary issues, since decisions in the relevant international fora are taken on the basis of weighted voting. It will be more difficult in other fora such as the WTO or the United Nations Framework Convention on Climate Change (UNFCCC), where the tradition is to operate through consensus. But it should not be impossible.

V. Conclusion

Has the G20 lived up to the expectations raised when it was established? The answer to this question can be unambiguously positive as far as the first two years are concerned, though its crisis management capacity will once again be tested by the Eurozone crisis.

The group can certainly claim to have succeeded in averting a prolonged global downturn through concerted, if not fully coordinated, policy action. It can also claim to have taken a number of initiatives to reform financial sector regulation and to strengthen the IFIs. It has also initiated an ambitious process for policy co-ordination

across countries which are widely regarded as an essential element for effective management of an interconnected global economy.

It can be argued that some of these policy decisions were relatively easy. The fact that the world was teetering on a precipice in early 1999 imparted a sense of urgency that something had to be done. The specific actions taken to counter the recession - fiscal and monetary expansion - were also politically popular, as they appeared to be responding to the need to protect jobs. The only critics were the anti Keynesians, warning about inflationary consequences several months ahead. The action taken to tighten financial regulation was also politically popular, as it resonated well with public anger at “greed in Wall Street”, which was seen as responsible for loss of jobs and the destruction of value in homes. The only dissenters were those who felt that excessive regulation might dampen flexibility and innovation, but they were willing to bide their time, and find ways to dilute the restrictive steps later.

The strengthening of the IFIs represented an agenda that had been on the table for some time, and while it had been resisted earlier, it is now seen as a relatively low cost way of helping developing countries, and also some of the new Eurozone members, to obtain finance to tide them over the crisis. Given the extraordinary amounts being used for bail outs in the industrialized countries, it would have been odd to deny much more modest amounts to help other countries.

The new Multilateral Assessment Process (MAP) which has the ambitious objective of bringing about effective coordination of macro policy across countries, is potentially very important but is still a work in progress. Unlike the other initiatives taken in the first two years, this does not represent a case of fixing the system where it is visibly broken. It is potentially a game changer. However, to be successful, it must produce a process which persuades sovereign governments to rethink their domestic policy options in the light of their global spill over effects, and in the light of some assurance that other countries will act in a manner to achieve an 'upside scenario'. It would be unrealistic to expect any easy victories here. Something like the MAP is necessary if we want to ensure continued viability of a highly interconnected global economy but, it will, at best, be a long haul, and countries should prepare themselves for a possibly rough ride.

Will the G20 be able to ensure a continuing good record of performance in the years ahead? This is a much more difficult question to answer since the problems the G20 now face are much more difficult. The 2008 crisis is over but the ongoing Eurozone crisis is in some ways more difficult. The first discussion of the outcome of the MAP at the summit level in Cannes in November 2011 will give some indication of how far the G20 can engage in meaningful discussion of difficult issues, involving decisions made by sovereign governments which have to pass the test of domestic political acceptability. It will also be the occasion to judge whether there is real appetite for considering structural reforms in the IMS.

Saving the Doha Development Round, which at present seems to be going nowhere, will require extraordinary political leadership. It could be argued that the G20 is not the right forum to discuss these issues, but on that consideration it

shouldn't be addressing many of the other issues either. If the Doha Development Round is important, it should be the responsibility of the G20 to try and restore momentum by giving a political push to what at present seems a hopelessly mired activity.

If the Doha Round is difficult, the Climate Change Negotiations, which are the next major ongoing item on the international agenda, are even more difficult. However, there is clearly more time to build a broader consensus on these issues.

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