Reshaping Global Economic Governance and the Role of Asia in the Group of Twenty (G20)

ADB

Peterson Institute for International Economics

© 2011 Asian Development Bank

All rights reserved. Published 2011.
Printed in the Philippines

ISBN 978-92-9092-283-4
Publication Stock No. RPT102850

Cataloging-In-Publication Data

Reshaping global economic governance and the role of Asia in the Group of Twenty (G20)
Mandaluyong City, Philippines: Asian Development Bank, 2011.

1. Global Economic Governance 2. Asia and the Group of Twenty (G20) I. Asian Development Bank.

The views expressed in this publication are those of the authors and do not necessarily reflect the views and policies of the Asian Development Bank (ADB) or its Board of Governors or the governments they represent.

ADB does not guarantee the accuracy of the data included in this publication and accepts no responsibility for any consequence of their use.

By making any designation of or reference to a particular territory or geographic area, or by using the term “country” in this document, ADB does not intend to make any judgments as to the legal or other status of any territory or area.

ADB encourages printing or copying information exclusively for personal and noncommercial use with proper acknowledgment of ADB. Users are restricted from reselling, redistributing, or creating derivative works for commercial purposes without the express, written consent of ADB.

Note:
In this report, “$” refers to US dollars.

Asian Development Bank
6 ADB Avenue, Mandaluyong City
1550 Metro Manila, Philippines
Tel +63 2 632 4444
Fax +63 2 636 2444
www.adb.org

For orders, please contact:
Department of External Relations
Fax +63 2 636 2648
adbpub@adb.org

Contents

Acknowledgments

This report is an outcome of the Asian Development Bank's (ADB's) Research and Development Technical Assistance project 7501, *Asia's Strategic Participation in the Group of Twenty (G20) for Global Economic Governance Reform*. The project was conceptualized, supervised, and coordinated by Cyn-Young Park under the overall guidance of Iwan Azis, Head of ADB's Office of Regional Economic Integration.

The report, jointly prepared by ADB and the Peterson Institute for International Economics (PIIE), draws on important lessons from the global financial crisis to offer policy recommendations in the areas of growth, finance sector reforms, international financial institution reforms, the link between global and regional financial institutions, global financial safety nets, trade, development, and energy and climate change. It also highlights the importance of Asia's active participation in global policy dialogue and reform initiatives. A team of PIIE research fellows led by Marcus Noland prepared background papers on key economic governance reform and policy issues while Cyn-Young Park coordinated similar efforts from ADB and other regional scholars. The contributors to these background papers include Douglas Arner, Iwan Azis, Taeho Bark, Yoon Je Cho, Joseph Gagnon, Morris Goldstein, Gary Hufbauer, C. Randall Henning, Trevor Houser, Moon Sung Kang, Jacob Kirkegaard, Cyn-Young Park, Edwin Truman, and Woan Foong Wong.

International workshops were held at Washington, DC, United States in April 2010 and Seoul, Republic of Korea in October 2010 to review and refine the background papers. Both ADB and PIIE organizers are grateful to all the speakers and participants from these two workshops for their valuable comments and suggestions. The organizers are also thankful to Yvonne Priestly for helping coordinate the Washington conference and to Ma. Theresa Robles for organizing the Seoul conference.

Rogelio Mercado provided excellent research assistance and data support. Robert Davis guided the project team in the publication process. Mitzirose Legal helped in the administration of this publication. Edith Creus designed the layout and artwork, and typeset the report.

Author:
Iwan J Azis (ija1@cornell.edu)

The Perspective from Developing Asia

Global Imbalances

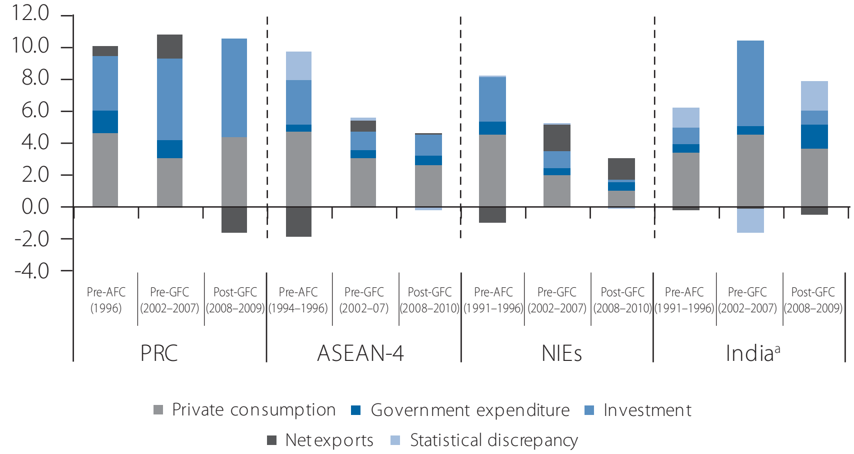
As the most dynamic region in the world, Asia has an important role to play in shaping the G20 agenda for balanced and sustainable growth. This requires Asia to help provide global public goods and to rebalance the global economy. From the Asian perspective, rebalancing translates into two strategic goals: increasing intraregional trade and stimulating domestic demand (see Adams, Jeong, and Park 2010). This is particularly relevant for East Asian countries. In the last few years, the region's trade pattern has been characterized by increased intraregional trade of intermediate inputs, while trade of final goods is mostly with industrial countries. A production network has emerged in a big way, where multinational companies can lower the cost of production by taking advantage of the proliferating free trade agreements (FTAs) in the region.

After the recent crisis, such a trade pattern cannot be sustained; alternative markets need to be found as the demand prospect from industrial countries becomes more uncertain. The alternative that makes sense is the region itself. For export-oriented economies, shifting entirely from external to domestic demand does not make sense, while for other economies, strengthening domestic demand is critical. Raising consumption should be the priority for the PRC, and raising investment is the most important challenge for the rest of Asia. Since early 2000, a major source of growth in most countries except the PRC has been private consumption, not investment **(Figure 8)**. This has caused the saving–investment imbalance to widen.

Why the low investment? Since the Asian crisis, most investors in the region have turned cautious and more conservative. The "usual suspects" also persist, i.e., institutional constraints, a less than favorable investment climate, and limited infrastructure. On the other hand, savings remain high and growing. Households in developing economies have strong precautionary motives to save, for, among other reasons, a lack of formal social safety nets. The corporate sector also has a high propensity to save because of various kinds of uncertainties. It is ironic that excess saving occurs when the region badly needs financing for new and improved infrastructure (see ADB and ADBI 2009).

Growing demand in industrial countries and low supply elasticity in the US mean strong growth of exports and continued trade surplus in export-oriented economies. This contributes to the widening

Figure 8 Sources of GDP Growth, by Expenditure Approach—Emerging Asia
(percentage points)



AFC = Asian financial crisis; ASEAN-4 = Indonesia, Malaysia, Philippines, and Thailand; GDP = gross domestic product; GFC = global financial crisis; NIEs = Hong Kong, China; Republic of Korea; Singapore; and Taipei,China; PRC = People's Republic of China.

Note: Aggregates are computed using gross national income (Atlas method, current US$) as weights. Values refer to period average.

[a] Based on constant factor prices.

Source: Staff calculations based on data from various issues of ADB *Key Indicators*, CEIC, *China Statistical Yearbook 2009*, national sources, and World Bank *World Development Indicators*.

of global current account imbalances. In terms of size, the imbalance is largest between the US and the PRC. Trade of the PRC with other Asian countries is generally in deficit, while imbalances of Asia excluding the PRC with industrial countries and the US are relatively small. Thus, the role of the PRC is critical as far as Asia's contribution to global imbalances is concerned.

An easy money environment was one of the important sources of global imbalances that fueled the recent crisis.[6] The fear of deflationary pressure associated with falling asset prices after the Asian financial crisis, the tech bust in 2000, and the looming Iraq war prompted the Federal Reserve to adopt an accommodative fiscal and monetary policy that caused not only excessive spending and a credit boom, including one in the housing market, but also raised US imports, particularly from Asia (Azis 2009). This exacerbated the already large US current account deficit caused by the growing fiscal deficit, especially since early 2000. The resulting

6 In its final report, the congressional commission of 10 members formed to investigate the causes of the crisis concludes that it was the result of "human action and inaction, not of Mother Nature or computer models gone haywire." The report clearly singles out the Federal Reserve for backing "30 years of deregulation." The report also points out that the IMF did appropriately stress the urgency of addressing large global current account imbalances that risked triggering a rapid and sharp decline in the dollar that could set off a global recession, although it failed to link these imbalances to the systemic risks building in financial systems (FCIC 2011).

appreciation of Asian currencies—albeit not all are fully flexible—and lower returns in industrial countries brought most capital back to Asia. Hence, a round-tripping pattern was established with high transaction costs. Market intervention by most Asian authorities then caused further accumulation of foreign reserves.[7] From this perspective, to deal with global imbalances, policies directed toward lowering the US fiscal deficit are as critical as other measures.

During the crisis, global current account imbalances actually narrowed as world trade volume also fell. Asia contributed to this encouraging trend: trade began to diversify, with intraregional trade expanding to include more Asian countries, while exports to non-Asian emerging markets increased as well. The current account surplus in many countries started to fall, and the largest source of growth was domestic demand. The PRC's 12th Five-Year Plan also put a strong emphasis on rebalancing demand toward domestic sources, particularly consumption. There is, however, no reason to believe that this trend of declining global imbalances will continue. The growth of global trade, which showed a V-shaped recovery in 2009–2010, has started to slow. Many forecasts also predict that global imbalances are likely to grow in the coming years (IMF 2010c). This is worrisome because the current recovery in many countries is fragile. From the recent crisis we have seen the severe damage that growing imbalances can create.

Rising oil prices raise further concerns, although G20 can actually resolve this matter in a more coordinated way since its members include both the world's largest oil producer and world's largest consumer. During the past decades we have seen several episodes of oil price increase and their impact on the world economy. Unlike in the past, however, the surge of oil prices that began in the fall of 2004 did not result in a major economic slowdown; at least not in any of the G20 countries. In oil-importing economies, the demand-driven nature of the oil price shock counteracted its adverse repercussions.[8] But the impact of the current oil price increase may be different. It may be more serious because many economies have just started to recover from the most severe crisis since the Great Depression, and because the recovery in Europe and the US is still fragile.

For poor Asian countries, this adds to the seriousness of the problem, since they are also struggling to cope with the rising food prices that raise poverty and malnutrition rates. Ironically, in many agriculture-based economies, rising food prices do not necessarily translate into higher incomes of farmers, that is, the farmers' terms of trade do not improve. While there may not be much that can be done to deal with the supply-side shock (weather-related), a policy reform in food production and distribution that will ensure the pass-through of food price increases to farmers' income can be proposed as part of the G20 development agenda.

---

[7] With rising costs of keeping a large amount of reserves, some Asian governments set up and use government-controlled investment companies to manage a portion of official foreign reserves to adjust portfolio composition.

[8] Most countries in Asia are net and oil importers, intensive in energy use, and are relatively inefficient in energy use; in some countries, however, the share of oil in total energy use is not that large.

Intraregional Trade and Exchange Rate Cooperation

The impact of a sharp fall in world trade during the crisis was particularly severe in export-oriented economies such as Japan, the Republic of Korea, the PRC, Malaysia, Singapore, and Thailand. Industrial countries including the US are important markets for their final goods exports, whereas intermediate goods are imported from other Asian countries. This pattern of trade has been one of the characteristics of the production network that has spread across East and Southeast Asia.[9] Although industrial countries made assurances during the London Summit that they would keep their markets open, it would be ill-advised for Asia to continue relying on markets in industrial countries for their final goods exports. With demand falling from the slow-growing industrial countries, intraregional trade in final goods is expected to increase. It is therefore important for the region to dismantle any barriers to intraregional trade.

A scenario where PRC consumers can take up lost US demand for products from Asia is unlikely in the short run. Freer trade among Asian countries is the only reasonable solution that will simultaneously deal with the problems of global imbalances. Here, the proliferation of FTAs among Asian countries is helpful.[10]

No less important is the stability of intraregional exchange rates. Evidence has shown that stable intraregional rates can help foster intraregional trade. After Lehman's collapse, interregional rates started to become more volatile and intraregional trade fell **(Figure 9)**.[11] External forces that are also at play caused volatility to continue. The second round of quantitative easing by the US Federal Reserve, aimed at preventing a possible deflationary spiral at a time of fiscal policy paralysis, is adding more pressures for capital to flow out from the US. Even before this second round was announced, interest rates in the US and other industrial countries were already low, triggering a wave of capital outflows. A substantial amount of these flowed into emerging Asia with its high returns, robust growth, stable macroeconomic conditions, and strong currencies. As shown in **Figure 10**, after dipping sharply during the crisis, capital has returned to the region. Even in net terms, the trend in ASEAN-4, the newly industrialized economies, and India showed a marked increase of inflows right after the crisis.

While the composition of capital flows varies across countries, rising portfolio investment puts strong pressure on exchange rates. The resulting dollar depreciation (Asian currencies' appreciation) led many countries to respond by either imposing capital controls or conducting

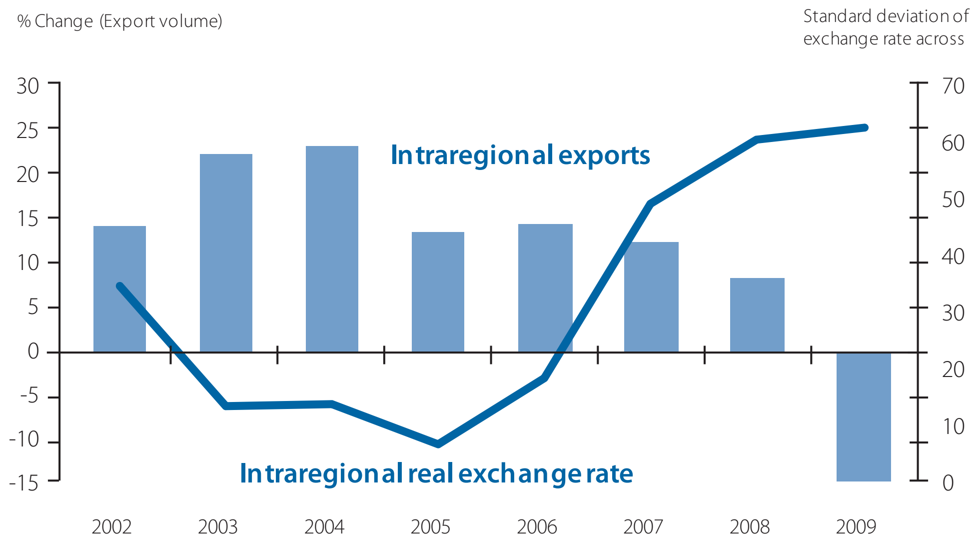
---

9 This production network has played an important role in forging the region's productivity.

10 Some agreements that cover all Asia are still elusive, and in some cases the pace of implementation remains questionable.

11 Greater intraregional exchange rate stability can also help reduce policy tension. It is, however, to the region's advantage if flexibility of their currencies against non-regional currencies is maintained. The flexibility is important for managing external shocks and further capital flows.

Figure 9 Intraregional Exports and Exchange Rate—Emerging East Asia



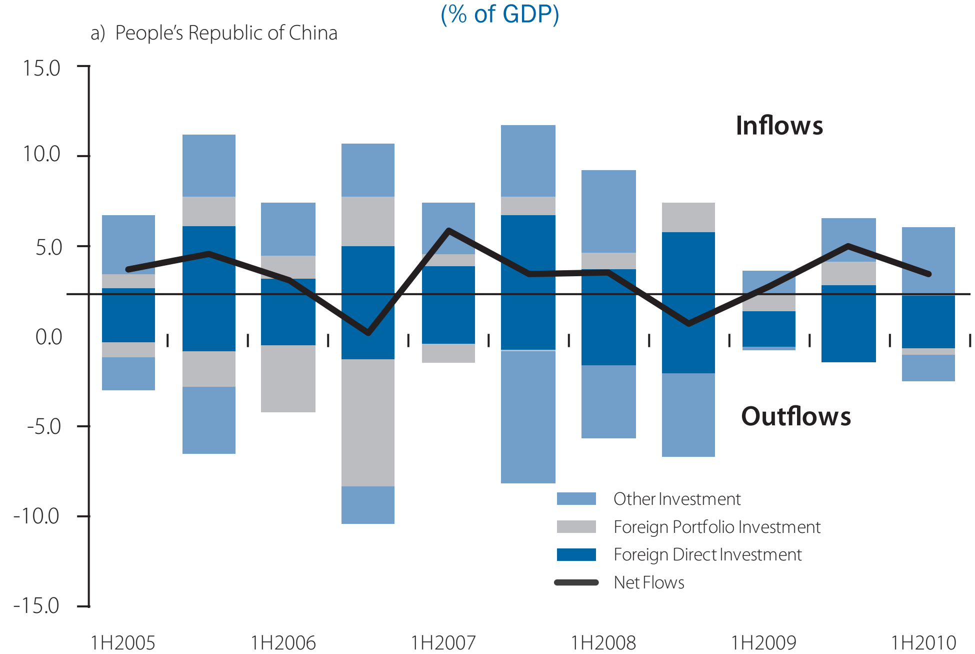
Emerging East Asia = Brunei Darussalam; Cambodia; People's Republic of China; Hong Kong, China; Indonesia; Republic of Korea; Lao People's Democratic Republic; Malaysia; Myanmar; Philippines; Singapore; Taipei,China; Thailand; and Viet Nam.

Note: The standard deviation of exchange rate is computed across countries and weighted using total trade (at constant 2005 US$ prices). Intraregional real exchange rate against the Asian Monetary Unit (ASEAN+3 including Hong Kong, China) was used. It does not include Taipei,China as data were unavailable.

Source: Research Institute of Economy, Trade and Industry (RIETI), Japan for real effective exchange rate; IMF *Direction of Trade Statistics* for exports; IMF *World Economic Outlook Database* and national sources for domestic and foreign income, and consumer price indexes; and World Bank *World Development Indicators* for gross national income.

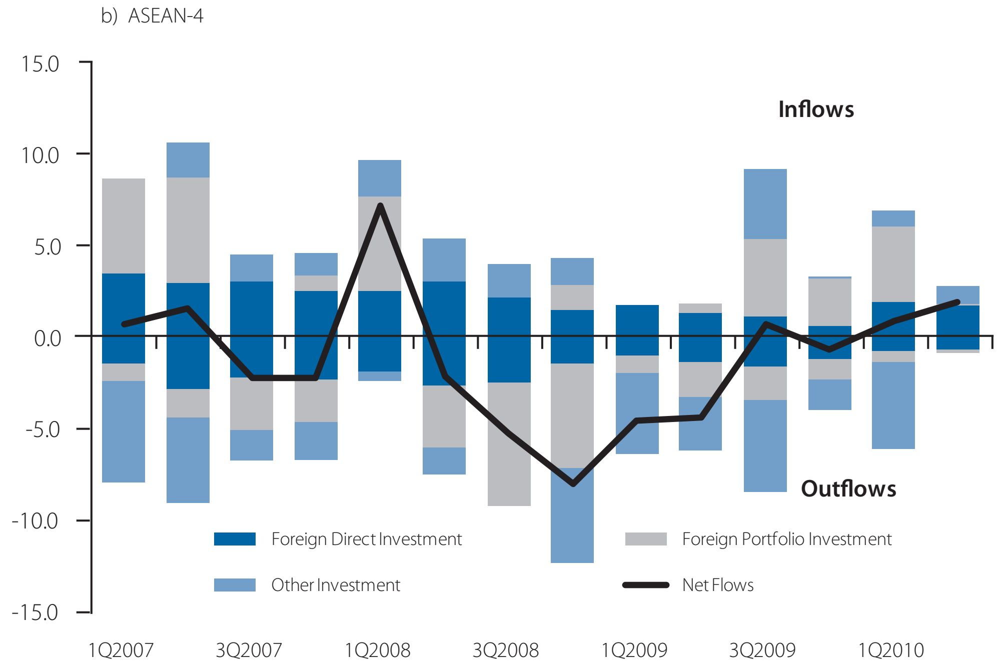
Figure 10 Financial Account Flows

(% of GDP)



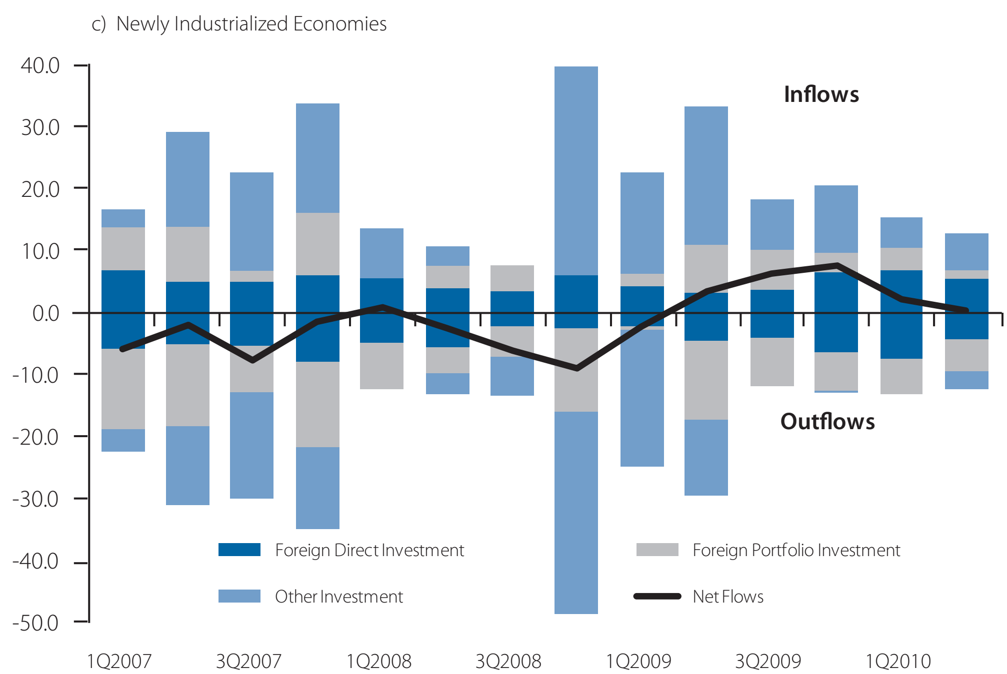
Source: OREI staff calculations using data from the International Monetary Fund and national sources accessed through the CEIC database.

Figure 10 *continued*



Note: Other investment includes financial derivatives. ASEAN-4 includes Indonesia, Malaysia, Philippines, and Thailand. Data for 2Q2010 excludes Malaysia.

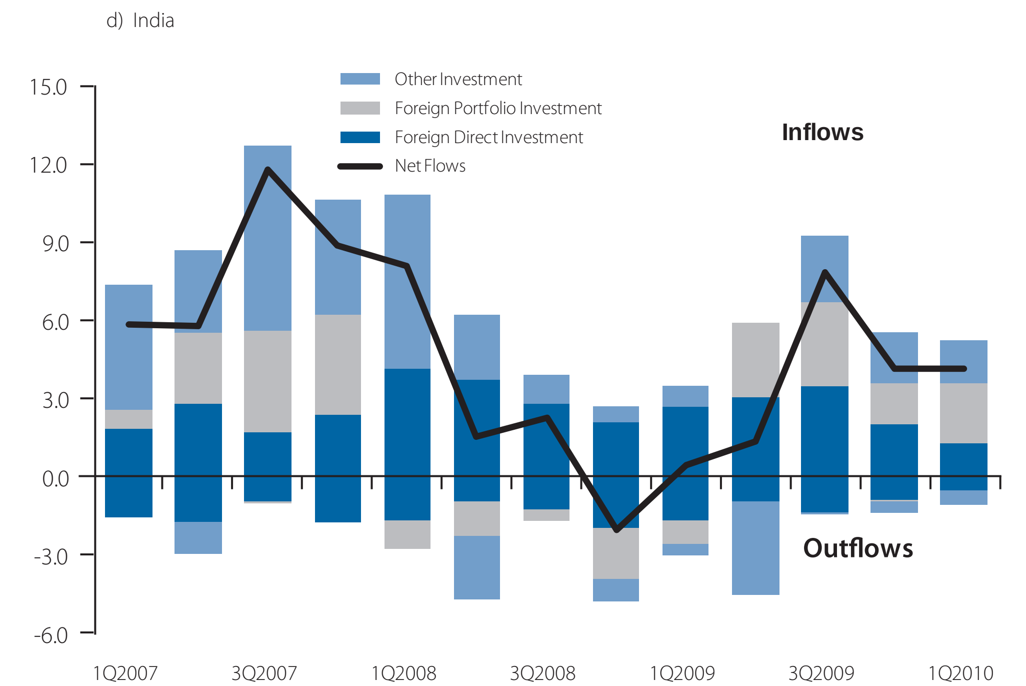
Source: OREI staff calculations using data from the International Monetary Fund and national sources accessed through the CEIC database.



Note: Other investment includes financial derivatives. Newly industrialized economies include Hong Kong, China; Republic of Korea; Singapore; and Taipei,China.

Source: OREI staff calculations using data from the International Monetary Fund and national sources accessed through the CEIC database.

Figure 10 *continued*



Source: OREI staff calculations using data from the International Monetary Fund and national sources accessed through the CEIC database.

exchange rate intervention. This makes efforts to maintain stability of intraregional exchange rates more difficult, but at the same time it opens up the possibility of policy coordination. Indeed, some countries in ASEAN+3, supported by the ADB, have initiated a series of discussions and policy dialogues on this issue.

The spillover effects of unilateral capital control, and awareness that it can potentially create distortion, also reinforce the need for cooperation. The fear of a sudden stop (as in 1997) is another source of concern. But the difficulty in finding an acceptable modality of cooperation due to the diversity of exchange regimes and associated political sensitivity may have put off any formal arrangement from emerging. A classic case of the prisoner's dilemma thus prevails.

Because the PRC's trade balance with most ASEAN countries is in deficit, a scenario of simultaneous exchange rate adjustment through cooperation will also make the realignment of the yuan easier. It may be more effective than pressuring a country to adopt a particular exchange system. Indeed, economists are not always in agreement as to what exchange rate system is best to adopt. While globally there has been a trend of increasing number of floaters, it remains unclear how to determine the extent to which a currency deviates from its equilibrium level.

Appropriateness of a particular regime depends on each country's conditions. The exchange rate system in Asia is diverse, ranging from a floating Japanese yen to a currency board system in Hong Kong, China (others are in between). Equally ambiguous is the precise definition and level of equilibrium exchange rate. While some currencies may be undervalued, the type and the extent of intervention considered acceptable remains a gray area. In the past, the IMF often supported efforts made by industrial countries to coordinate their monetary and fiscal policies that could alter the exchange rate in the name of maintaining global financial stability.[12]

While exchange rate cooperation is warranted, Asia is likely to shy away from a strong form of cooperation or other forms that require strong institutions (such as monetary union or common currency). The recent sovereign debt crisis in Europe made the benefit of having such arrangements doubtful. Also, Asia does not have a good track record of institution-heavy economic cooperation.[13] But there is still a whole spectrum of options to select, ranging from a basket system that can be designed to avoid the "N-1" problem, to Bretton Woods–like systems where countries directly peg their currencies to each other and let them float jointly against other currencies, say, the US dollar (similar to what happened in Europe before a common currency was adopted and managed by a supranational body, the European Central Bank). The rates against a regional basket such as the Asian Monetary Unit (AMU) can also be used as a reference zone, certain deviations from which will trigger some policy measure. The lightest form of arrangement would be simply to enhance policy dialogue among member countries, for example through the existing Economic Review and Policy Dialogue forum. After the Chiang Mai Initiative was multilateralized in early 2010 (to become CMIM), finance ministers of ASEAN+3 made a decision to establish an independent surveillance unit, the ASEAN+3 Macroeconomic Research Office. This marks the region's first step toward institutionalizing financial cooperation. It is likely that exchange rates and capital flows will be part of that office's surveillance analysis, along with other macroeconomic issues.

Another related source of concern is the declining value of the US dollar. Many Asian countries worry that rising commodity prices and a soaring US deficit to pay for stimulus can lead to higher inflation that will undercut the value of their US dollar-denominated reserves. The PRC and Japan are the largest holders of US Treasury bills. No wonder that on several occasions PRC officials questioned profligate US spending habits. It is in this context that ideas were floated that Asians either need their own currency or should adopt a currency basket to replace the dollar. Actually such a proposal was raised right after the Asian financial crisis, but the recent trend may have strengthened its rationale—and it may quicken the process. Looking at currency movements in selected Asian countries, over the last few years reliance on the dollar has been declining,

---

12 At least the IMF does not place any obligations on those countries when they conduct such efforts.

13 Even during the recent crisis, the Chiang Mai Initiative was not used.

and the role of other currencies, including the yen and yuan, has increased. This occurred without any announcement about a basket system. But to move to the next step, closer policy coordination is obviously needed.

Through the G20, Asia can learn from the experience of other G20 countries—in Europe in particular—in policy coordination and exchange rate cooperation. By realizing the differences between the two sets of economies, lessons can be learned as to what policy direction to take, what not to take, and what needs to be done. The speed and nature of each stage and the components of cooperation can be studied, and when found relevant to the Asian context, they can be emulated.

Domestic Demand and Interactions with Development Issues

From Asia's perspective, giving a more prominent role to development issues in the G20 agenda, as decided at the Seoul Summit, is commendable. One of the G20 development initiatives highly relevant for Asia is financial inclusion. Through the Financial Inclusion Experts Group, nine Principles for Innovative Financial Inclusion were announced at the Toronto Summit. The principles, from leadership to regulatory framework, are intended to form the basis of a concrete action plan for improving access to financial services for the poor, details of which were released at the Seoul Summit. Two broad agenda have been selected: access through innovation, and finance for small and medium-sized enterprises.

But G20 also covers other development issues, many of which are relevant for Asia as well. Most governments in Asia realize the need to strengthen social safety nets, including pension and health insurance programs; speed up the development of physical infrastructure to reduce supply bottlenecks; and raise investment for more sustainable long-term growth, such as energy efficiency, renewable and clean energies, green transportation, and quality-of-life services (health care and sanitation). All these are not inconsistent with rebalancing. Strategies have been discussed and designed, measures have been taken, and some may not be the most optimal and their implementation may face many bottlenecks, especially when macro and fiscal policy is inconsistent with more development-oriented measures such as these. Still, any strategies and policy measures (including those directed toward lowering global imbalances and mitigating their impact) ought to be linked with the ultimate goal of welfare improvement. The effectiveness of those policies needs to be evaluated based on indicators that go beyond the narrow macroeconomic and financial sector.

Indeed, while development issues are diverse and by themselves deserve attention, little has been done to understand the interactions between these issues and macro, financial, and trade measures in the context of Asia's efforts to rebalance. Thus, exclusion of the poor and small and medium-sized enterprises from financial services, issues of the environment and climate change, income inequality and poverty—all of which are so critical in many G20 countries—should not be seen only as the consequential impact of macro-financial measures that will be subsequently countered by some compensating policies (such as financial inclusion). Yet this practice is common, instead of attempts to reassess the respective macro-financial policy and explore an alternative that will ensure inclusion.

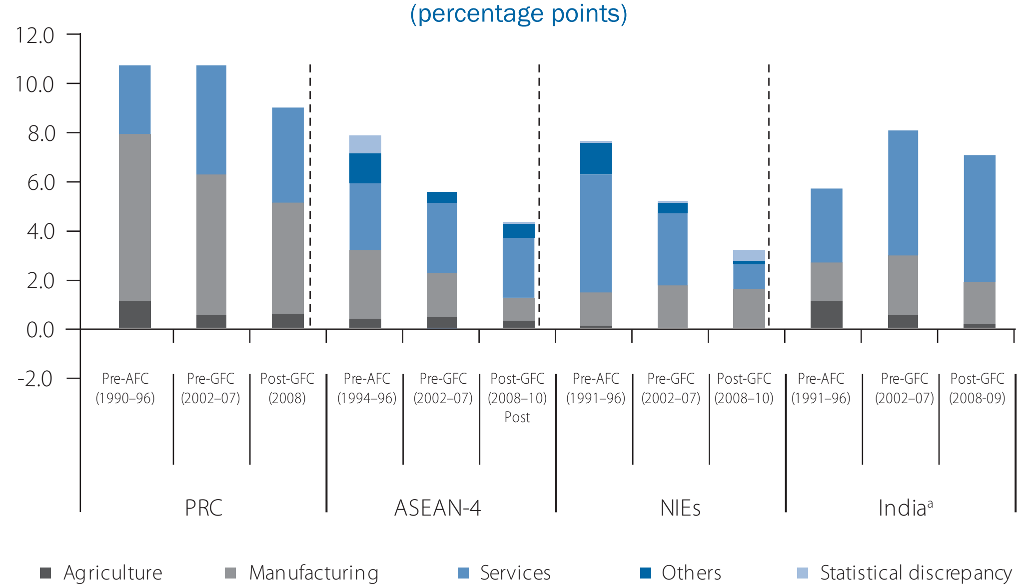
Interactions imply two-way directions. A proactive rather than reactive approach suggested above is not only preferable in terms of cost-effectiveness, but it can also preclude any possible negative feedback effects. For example, a deteriorating environment due to an unsustainable pattern of development in many Asian countries can have an adverse impact on the supply and productivity of many sectors in the economy, and it can contribute to the increase of food prices, commodity prices, and inflation in general. Rising inequality across any country in Asia is likely to have an adverse impact on growth, hence its sustainability. The mechanisms of this can work through at least three channels: uncertainty caused by greater social instability, insecurity due to lack of property rights, and rent-seeking practices that can raise transaction costs and so dampen growth. Although the impact may not be felt in the short run, when output growth falls, so will household income, including those in the low-income bracket. When inflation rises and a food crisis looms, poverty incidence tends to increase.

Excess saving and the link between financial sector development and broader development issues is another noted example. According to flow-of-funds data, most countries in Asia have excess saving in the sense that total saving exceeds actual investment in the real sector. This excess largely goes to financial assets, both abroad (foreign reserves in US treasuries) and at home (equity, bonds, and other securities). As a result, economic growth is strongly supported by a growing financial market. This is also consistent with the information from national income accounts where the financial sector is recorded as one of the major sources of growth, along with domestic trade and other services **(Figure 11)**. Except during the Asian financial crisis, this pattern has been persistent and self-reinforcing, as incentives to invest in financial assets continue to exceed those to invest in the real sector. Although this may foster overall growth and financial sector development, it fails to provide sufficient employment opportunities. This can spell trouble in some countries in Asia where the labor force is growing fast. Consequently, an unchanged rate of output growth creates much less employment now than in the past (declining employment elasticity). The same applies to poverty reduction (declining poverty elasticity).

Thus the challenge for Asia is how to channel the excess saving toward more productive investment in a manufacturing sector that will generate jobs, since this is generally more employment-creating than services in general. This is why improvements in the business and investment climate are so important. From this perspective, efforts to raise domestic demand are not only necessary for lowering global imbalances, but for many Asian countries they are also warranted to make development and growth more inclusive (Zhuang 2009).

Figure 11 Sources of GDP Growth, by Sector—Emerging Asia

(percentage points)



AFC = Asian financial crisis; ASEAN-4 = Indonesia, Malaysia, Philippines, and Thailand; GDP = gross domestic product; GFC = global financial crisis; NIEs = Hong Kong, China; Republic of Korea; Singapore; and Taipei,China; PRC = People's Republic of China.

Note: Aggregates are computed using gross national income (Atlas method, current US$) as weights. Values refer to period average.

[a] Based on constant factor prices.

Source: Staff calculations based on data from various issues of ADB *Key Indicators*, CEIC, *China Statistical Yearbook* 2009, national sources, and World Bank *World Development Indicators*.

Indeed, the growth pattern in many Asian countries has been far from being inclusive. While the region has done relatively well in terms of output growth and macroeconomic management, even during the recent crisis, the development and welfare outcome has not been good. In many countries environmental conditions have worsened, resource depletion has become alarming, unemployment (especially among youth and the educated segment of the labor force) has increased sharply, and income inequality has risen almost across the aboard. To be credible and accepted by the global community, G20 needs to assume leadership in this area. It should encourage policy makers to seriously reassess the development pattern that has produced unfavorable outcomes. In particular, focus ought to be directed toward the interactions of these issues with the strategy and policy approach needed to lower and mitigate global imbalances. This is the only way to achieve "strong, sustainable, and balanced growth"—the stated goal of G20.

Global Role and Governance

In Chinese, the word "crisis" is made up of the characters for "danger" and "opportunity." From Asia's perspective, the G20 should see the recent crisis as these two things. The fact that the global recovery is "strengthening, but is still uneven" and that the international monetary system has proven "resilient, but vulnerabilities remain" indicate that the work is only half done. Emerging economies have become important forces in helping the world to weather the crisis, and this highlights the importance of the G20. Indeed, the G20 has done remarkably well in helping the global economy to recover. It has emerged as the leading forum for coping with the crisis. But the unevenness of the recovery and the persistent vulnerability in the global financial system remain serious challenges. Financial regulations have been strengthened but are still far from sufficient to avert a similar shock in the future, especially when "too big to fail" problems remain. Many components need further structural changes, especially those related to the least regulated financial instruments. For Asian countries, the lesson of the Asian financial crisis is clear—that a too liberalized financial sector not supported by proper regulation and supervision is a recipe for disaster. Whether the world economic structure of the past, as characterized by liberalization and deregulation, can realize a smooth transformation of the global economy to achieve more sustainable and balanced growth with minimum risk of crisis, depends on how far the G20 can help to push reforms of the international monetary system. The recent crisis should be seen as an opportunity to push such moves.

The unevenness of growth and the difficulties in achieving more significant finance sector reform present another difficult challenge as it touches on the issue of power influence. The role of the IMF in reporting the vulnerabilities prior to the crisis is a notable example. Despite the IMF's warning, officials from powerful industrial countries concealed such important information and put pressure on the IMF to tone down warnings before the crisis. Often the IMF wilts in the face of officials' demands to water down criticisms.[14] One cannot imagine that being true for developing and emerging countries. The extent to which the G20 can balance the influence between the developed world and emerging economies is a major test for the future development of this global forum. Another critical test is whether it can properly handle its relationship with non-G20 countries.[15] Unless it listens and caters to their claims and respects their interests, its legitimacy—and perhaps its existence—will be seriously questioned.

Asians are coming of age. In formulating the strategy to support its agenda, the G20 can absorb the experience in Asia that may provide lessons to be shared, both good and bad, on macroeconomic and development policies. In addition to providing financial resources, Asian members of the G20 can also play a greater role in helping to set the vision and ambitions

---

[14] Revealed in a report by the IMF's Independent Evaluation Office (IEO) in January 2011. In some cases, according to the report, so intimidated were the IMF staff that they did not challenge the officials' arguments. *See* IMF 2011.

[15] G20 member countries only account for 10% of more than 200 states that engage in global economic activity.

for global rebalancing, and to share Asia's unique experience in areas such as establishing international production networks, and using the government and public sector to play a vital role in supporting these networks.[16] In the global financial reform, Asia should no longer be content to leave it to powerful industrial nations to decide; it must join in setting new standards for global financial institutions and in regulating risk. Regional or subregional arrangements can be used to facilitate Asia's stronger voice and sense of ownership.

The new global economic governance structure will need to be based on representative institutions that reflect the changing economic weight of emerging economies in the global economy. Asia should and will play a greater role on the global stage.

[16] The way the region looks at the importance of investment and the necessary infrastructure, beyond just trade, by establishing international production networks is acknowledged by many countries and institutions, including the Inter-American Development Bank. It suggests that Asia has a unique track record in establishing such production networks. Asia also has much to offer in terms of resources management, innovative financing, technical expertise on engineering and design, and project management.

References

Adams, C., H. Y. Jeong, and C.-Y. Park. 2010. Asia's Contribution to Global Rebalancing. *ADB Working Paper Series on Regional Economic Integration* No. 58. Manila: Asian Development Bank.

Arner, D., and C.-Y. Park. 2010. Global Financial Regulatory Reforms: Implications for Developing Asia. *ADB Working Paper Series on Regional Economic Integration* No. 57. Manila: Asian Development Bank.

ADB (Asian Development Bank) and ADBI (Asian Development Bank Institute). 2009. *Infrastructure for a Seamless Asia.* Manila: Asian Development Bank.

ADBI (Asian Development Bank Institute). 2010. Global and Regional Financial Safety Nets: Challenges and Policy Options. Prepared for the Republic of Korea G20 Presidential Committee. Unpublished.

Azis, I. 2009. Crisis, Complexity, and Conflict. London: Emerald.

Bank for International Settlements Statistics. www.bis.org/statistics/eer/index.htm

Bark, T., and M. Kang. 2011. Asia's Strategic Participation in the Group of Twenty for Global Economic Governance Reform: From the perspective of International Trade. *ADB Working Paper Series on Regional Economic Integration No. 74.* Manila:Asian Development Bank.

Brooks, D., R. Hasan, J.-W. Lee, and H. Son. 2010. Closing Development Gaps: Challenges and Policy Options. *ADB Economics Working Paper Series* No. 209. Manila: Asian Development Bank.

Carmassi, J., and R. J. Herring. 2010. The Corporate Structure of International Financial Conglomerates: Complexity and Its Implications for Safety and Soundness. In Berger, Molyneux, and Wilson, eds. *The Oxford Handbook of Banking*. Oxford: Oxford University Press.

Cho, Y. J. 2011. What do Asian Countries Want the Seat at the High Table for G20 as a New Global Economic Governance Forum and the Role of Asia. *ADB Working Paper Series on Regional Economic Integration No. 73.* Manila: Asian Development Bank.

Cohen, R., and M. Goldstein. 2009. The Case for an Orderly Resolution Regime for Systematically-Important Financial Institutions*. Financial Reform Project Briefing Paper* 13. Washington, DC: The Pew Charitable Trusts Financial Reform Task Force.

FCIC (Financial Crisis Inquiry Commission). 2011. Conclusions of the Financial Crisis Inquiry Commission. www.fcic.gov/report/conclusions

FSB (Financial Stability Board). 2010. Principles for Reducing Reliance on CRA Ratings. www.financialstabilityboard.org/publications/r_101027.pdf

Gagnon, J. 2010. *Current Account Imbalances and the Global Recovery: Major Policy Changes Needed*. Washington, DC: Peterson Institute for International Economics. 3 September.

Goldstein, M. 2009. Confronting Asset Bubbles, Too Big to Fail, and Beggar-Thy-Neighbor Exchange Rate Policies. *Policy Briefs in International Economics* 10-3. Washington, DC: Peterson Institute for International Economics.

———. 2010. Integrating Financial Regulatory Reform with Reform of the International Monetary System. Paper for the Joint Asian Development Bank and the Peterson Institute for International Economics conference on Reshaping Global Economic Governance and the Role of Asia in the G20. Seoul. 26–27 October.

G20 (Group of 20). 2008. Declaration Summit on Financial Markets and the World Economy. www.g20.org/Documents/g20_summit_declaration.pdf

———. 2010. Seoul Development Consensus for Shared Growth. http://media.seoulsummit.kr/contents/dlobo/E3._ANNEX1.pdf

Haldane, A. 2010. The $100 Billion Question. Comments at the Institute of Regulation and Risk, Hong Kong, China. 30 March. http://www.bis.org/review/r100406d.pdf

Hanson, S., A. Kashyap, and J. Stein. 2010a. A Macroprudential Approach to Financial Regulation. Paper prepared for the *Journal of Economic Perspectives.* First draft. July.

———. 2010b. *An Analysis of the Impact of "Substantially Heightened" Capital Requirements on Large Financial Institutions*. University of Chicago Booth School of Business and Harvard University. May.

Henning, C. R. 2010. Connecting Regional and Multilateral Financial Institutions. Paper for the Joint Asian Development Bank and the Peterson Institute for International Economics conference on Reshaping Global Economic Governance and the Role of Asia in the G20. Seoul. 26–27 October.

Houser, T. 2010. A Role for the G20 in Addressing Climate Change? *PIIE Working Paper* Series 10-15. Washington, DC: Peterson Institute for International Economics.

Hufbauer, G. C., J. Kirkegaard, and W. F. Wong. 2010. G-20 Protection in the Wake of the Great Recession. Report to the International Chamber of Commerce Research Foundation. Washington, DC: Peterson Institute for International Economics. June.

IEA, OPEC, OECD, and World Bank (International Energy Agency, Organization of the Petroleum Exporting Countries, Organisation for Economic Co-operation and Development, and World Bank). 2010. Analysis of the Scope of Energy Subsidies and Suggestions for the G-20 Initiative. Joint report prepared for the G-20 Summit Meeting. Toronto. 26–27 June. www.g20.org (accessed 1 September 2010).

IMF (International Monetary Fund). 2010a. *World Economic Outlook Database*. October. www.imf.org/external/pubs/ft/weo/2010/02/weodata/index.aspx

———. 2010b. G-20 Mutual Assessment Process—IMF Staff Assessment of G-20 Policies. October. www.imf.org/external/np/g20/pdf/111210.pdf

———. 2010c. Global Economic Prospects and Policy Challenges. Prepared for the Meeting of G20 Finance Ministers and Central Bank Governors. http://www.imf.org/external/np/g20/pdf/060410.pdf

———. 2011. IMF Performance in the Run-Up to the Financial and Economic Crisis: IMF Surveillance in 2004-2007. Prepared by IMF's Independent Evaluation Office. www.ieo-imf.org/eval/complete/pdf/01102011/Crisis_Report_English.pdf

Krugman, P. 2010. Chinese New Year. *New York Times,* 1 January.

Mussa, M. 2008. IMF Surveillance over China's Exchange Rate Policy. In Morris Goldstein and Nicholas R. Lardy, eds. *Debating China's Exchange Rate Policy.* Washington, DC: Peterson Institute for International Economics.

Rhee, C. 2010. G20 MAP: A New Paradigm of the Global Economic Cooperation. Discussion paper for the Korea–Peterson Institute for International Economics G20 Conference. Washington, DC. 13 September.

Rottier, S., and N. Véron. 2010. The New Disintegration of Finance. *Financial Times.* 10 September.

SaKong, I. 2010. The G-20 Summit: Looking Back at Toronto and Forward to Seoul. Speech at the Peterson Institute for International Economics on behalf of the Korean Presidential Committee for the G20 Summit. Washington, DC. 30 June.

Strauss-Kahn, D. 2010. Crisis and Beyond—The Next Phase of IMF Reform. Prepared remarks delivered at the event The IMF in a Transformed World Economy. Peterson Institute for International Economics. Washington, DC. 29 June.

Summers, L. H. 2008. Commentary in Morris Goldstein and Nicholas R. Lardy, eds. *Debating China's Exchange Rate Policy.* Washington, DC: Peterson Institute for International Economics.

Truman, E. M. 2010a. *Sovereign Wealth Funds: Threat or Salvation?* Washington, DC: Peterson Institute for International Economics.

———. 2010b. The G20 and International Financial Institution Governance. *PIIE Working Paper Series* 10-13. Washington, DC: Peterson Institute for International Economics.

World Bank. 2009. What is Inclusive Growth? *PRMED Knowledge Brief.* Washington, DC: World Bank.

Zhuang, J. (ed.) 2009. *Poverty, Inequality, and Inclusive Growth in Asia: Measurement, Policy Issues, and Country Studies*. Manila: Asian Development Bank.

Reshaping Global Economic Governance and the Role of Asia in the Group of Twenty (G20)

This report, jointly prepared by ADB and the Peterson Institute for International Economics, aims to provide strategic guidance for emerging Asia's participation in the G20 and related discussion about reform of global economic governance. The recent global financial crisis underscored the fact that the spirit of cooperation is key to successful reform. Without tighter coordination between old and emerging powers, it will be hard to find lasting solutions to pressing global problems. The rise of emerging market economies heralds a new world order. Yet consolidating the new voices and soliciting a sense of ownership from them pose a real challenge. This report draws on important lessons from the crisis to offer policy recommendations in areas of imminent challenge confronting the leaders from both old and emerging powers.

About the Asian Development Bank

ADB's vision is an Asia and Pacific region free of poverty. Its mission is to help its developing member countries reduce poverty and improve the quality of life of their people. Despite the region's many successes, it remains home to two-thirds of the world's poor: 1.8 billion people who live on less than $2 a day, with 903 million struggling on less than $1.25 a day. ADB is committed to reducing poverty through inclusive economic growth, environmentally sustainable growth, and regional integration.

Based in Manila, ADB is owned by 67 members, including 48 from the region. Its main instruments for helping its developing member countries are policy dialogue, loans, equity investments, guarantees, grants, and technical assistance.

Asian Development Bank
6 ADB Avenue, Mandaluyong City
1550 Metro Manila, Philippines
www.adb.org
ISBN 978-92-9092-283-4
Publication Stock No. RPT102850

Printed on recycled paper

ISBN 978-92-9092-283-4

Printed in the Philippines