

THE BROOKINGS INSTITUTION

THE LONDON SUMMIT:
CAN THE G-20 FIX THE FINANCIAL CRISIS?

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PARTICIPANTS:

Introduction:

STROBE TALBOTT
President, The Brookings Institution

Moderator:

WILLIAM ANTHOLIS
Managing Director, The Brookings Institution

Featured Speakers:

MICHAEL FROMAN
Deputy National Security Advisor for
International Economic Affairs

KEMAL DERVIŞ
Vice President and Director, Global Economy and Development
The Brookings Institution

CARLOS PASCUAL
Vice President and Director, Foreign Policy
The Brookings Institution

ESWAR PRASAD
Senior Fellow, The Brookings Institution
Professor, Cornell University

JOHANNES LINN
Senior Fellow and Executive Director
Wolfensohn Center for Development
The Brookings Institution

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PROCEEDINGS

MR. TALBOTT: Okay. Our panelists are wired and ready to go. I'm Strobe Talbott and it's my pleasure to welcome all of you here to a very important event. Even by the standards of these extraordinarily busy times, I think it's safe to say that this is an especially important high stakes, and I would even say high suspense week.

The London Summit or the so called G-20, which starts on Thursday, is going to be a double test. It is going to be a test of the international community's willingness and ability to step up to the challenge of ending the global recession and beginning a global recovery, and doing so in an internationally coordinated fashion.

It's also going to be a big test for President Obama and his ability to reassert America's leadership role in this whole process, and that's going to mean harnessing the considerable popularity that he enjoys around the world, but at the same time, overcoming skepticism about some of his policy prescriptions. And these two challenges, the one for the world community as a whole and for the American President in particular are closely linked. We have an exceptionally well qualified panel to help us assess the chances for success, and perhaps even to define what success might mean for the G-20. Special thanks to Michael Froman. He is, as I think all of you know, Deputy Assistant to the

President, Deputy National Security Advisor for International Economic Affairs.

He is the White House liaison, not only to the G-20, but also to the G-7/G-8. And I would stress, he is very much a friend of Brookings institutionally and a personal friend of quite a number of us here. In fact, he is such a good friend that he has ducked out of his office on a very busy day when he's trying to get ready for a trip and pack and be on an airplane tonight to spend a half an hour with us, and he will have to leave after half an hour. He assures me that you should not take that as a walk-out, any objection to what he hears, although if he has a grouchy look on his face and he shakes his fist as he leaves, then I guess we'll have to reassess that, and he and I will try to smooth things over later.

This is a particularly important event and day for Brookings in another regard, as well, and that is, this is Kemal Derviş' first day as our colleague here at Brookings. He, until recently, as I think everyone in the room knows, was the Administrator of the United Nations Development Program. He is, as of today, the Vice President of the Institution and the Director responsible for our program on Global Economy and Development. In that capacity, he succeeds Lael Brainard, who was nominated by President Obama to be the Undersecretary of Treasury for International Affairs.

Kemal brings to Brookings many distinctions and accomplishments, the extraordinary work that he did at the UN, before that at the World Bank, in his native Turkey, and also his scholarship and his experience in a practical way in the realm of global governance.

That is a phrase, a concept, and an enterprise that is under stress right now. It's a phrase, a concept, and an enterprise that is going to be put on trial in London. And it is an enterprise that must not only survive the tests ahead, but most continue and rise to higher levels if we're going to get out of the multiple messes that we are in as an international community.

The G-20, for all of its deficiencies, including in its name and the imprecision of that number that comes after the hyphen, may not be the last best hope for global governance, but it is definitely the next best hope, and the stakes are very high. Like Mike Froman, Kemal is very much part of the solution, like Mike, he is a G-20 sherpa, and he, too, tonight will be flying to London to prepare the way for Ban Ki-Moon and advise the Secretary General of the UN at the London Summit.

Just a few words about the other Brookings scholars on the panel. Carlos Pascual, Vice President and Director of our Foreign Policy Program, also is the moving force behind our Managing Global Instability project which deals with the substance of global challenges, as well as

some of the process and institution questions, such as the G process and what numbers should come after the hyphens and all of the variable geometry that goes into global governance.

Eswar Prasad is a Senior Fellow focusing on Global Economics and Emerging Markets. He has been tracking G-20 stimulus plans across the world, and I recommend that you take a look at our web site to see this interactive feature that he's put together on that subject.

Johannes Linn is the Executive Director of the Wolfensohn Center for Development. Along with his colleague here at Brookings, Colin Bradford, Johannes was among the earliest advocates of a G-20 at the leader's level. So it must be particularly gratifying for him to see that concept now coming into reality. Finally, Bill Antholis, the Managing Director of Brookings, will serve as the Moderator. Bill helped the White House coordinate two G-8's back in the 1990's. He's written on several issues that are on the agenda today, including climate change, as well as having done some very important work on an over arching issue of critical importance, which is the need to be much more aggressive and successful in constituency building at home for international agreements that are necessary to protect free trade, grapple effectively with climate change, and press ahead with the struggle against global poverty.

All those are urgent priorities that must not be deferred because of the financial crisis and that I'm sure is a subject that will come up during the discussion. So, Bill, I will now turn the proceedings over to you.

MR. ANTHOLIS: Thanks, Strobe, and thank you all for coming. It's a pleasure to be here again with all of you and with this terrific panel, and obviously, with our newest colleague, Kemal Derviş, but also with an old colleague and friend, Mike Froman. Mike was part of an Opportunity 08 series that we had here at Brookings in the run-up to the presidential elections on our Bipartisan Advisory Council, and it's terrific for the first time to see you back here since then, Mike, and in your new U.S. government garb.

So the quick question to you is, what can we expect of this big meeting? We're still in the battle phase of addressing the global financial and economic crisis. There's been a lot of talk about stimulus in the United States, it's happened in China, as Eswar has tracked, it hasn't happened in some other places, but there are also regulatory issues and other issues on the agenda. What should we be looking to see come out of this?

MR. FROMAN: First of all, thank you, and it's good to be here with so many friends like Strobe, and Bill, and Kemal, and Pascual

and the others, Carlos and the others. First, let me say I don't think I need to say to this audience that we're in the midst of one of the worst financial and economic crises in several generations. It's a global crisis and it requires a global solution, and that really is the purpose of this G-20 meeting this week.

The agenda is two-fold, managing this crisis and preventing future crises like this from emerging again, and that means restoring growth, on one hand, and embarking on a whole series of regulatory and institutional reform efforts on the other. Restoring growth has at least four components; one is putting in place significant stimulus, fiscal and monetary, as you mentioned; two is, very importantly, fixing the financial systems of each of our countries and getting lending going to support the economy; three, avoiding protectionism; and fourth, taking steps to make sure that the international financial institutions have the resources and the tools they need to minimize the spread of the crisis to emerging markets and developing countries or to mitigate the impact of the crisis on those countries. I think you'll find that the agenda of the G-20 is robust in all of those areas.

The second track is the regulatory and institutional reform track. In there, there's a long list of work programs that came out of the Washington Summit last November, and further work that's been done in

any number of areas. And there will be work on expanding the scope of regulation, to take into account all systemically important institutions, markets, and products; there will be efforts to encourage offshore financial centers to abide by internationally recognized norms and rules; there will be progress made on capital and how capital is thought of for financial institutions, making sure the capital requirements prevent crises from developing, but also don't exacerbate the crises when they do develop; and there will be a series of institutional reforms from expanding the financial services forum, to reforming the international financial institutions, to creating methods for regulators and supervisors to cooperate with each other to deal with the global financial institutions that engage in cross-border activity.

I think it's a robust agenda, there is broad consensus on the nature of the agenda, and I think it should be a very productive meeting.

MR. ANTHOLIS: Maybe with that, turn to Kemal. Kemal is going to be acting as Secretary General Ban Ki-Moon's sherpa in the process. Do you see the set of issues on the table in the same way, are you sensing a sense of progress and this is another positive step in direction of the crisis, or does it feel like it's still out there?

MR. DERVIŞ: Well, it's still very challenging, but I do fully agree with, you know, Mike's outline of the agenda. I do believe there's

still – a lot of work has always happened in these meetings, as you well know, in the last 48 hours, and I think we'll be very busy in the next 48 hours. I do want to make perhaps two points in addition to Mike's agenda, because, you know, he presented it perfectly in terms of what is actually going to happen, but maybe two dimensions; one is maybe a note of optimism, because at the end of today, on the supply side of the world economy, you know, things actually should look good. Technology is advancing, the technological frontier is shifting outward, there's accelerated diffusion of knowledge, investment in many parts of the world, particularly in Asia, of course, is at historical highs, in systems that are quite deficient.

We've had the, you know, the ex-Soviet Union investing a huge amount of income very inefficiently, but now, you know, in a much more market oriented setting, emerging markets are investing a lot of their resources. So it's a demand collapse that was generated by the financial sector. But the underlying fundamental supply side aspects of the world economy are strong. So what we have to do is to fix the demand side, fix the fiscal stimulus and fix the financial sector, and once that's done, once we can do that, I personally think growth in the world can resume and can be quite rapid and everybody can benefit, particularly the poorest.

The second point I want to make, it is very important that the fiscal and banking measures extend to the emerging markets. The emerging markets individually, I'm not including China, China individually is systemically important, but individual countries in the emerging market world are not, but if you take them as a group now, they are close to one-third of world GDP. So allowing the crisis to spread into the emerging markets, to Latin America, to the Mediterranean, to parts of Asia, to Eastern Europe, having a huge demand collapse taking place there adding to the collapse we have in the rich countries will make things infinitely worse. So one of the big challenges, and that was the last point that Mike made, is to make sure that the global policies are truly global, that the recovery program is truly global and extends to the emerging markets and to developing countries.

Perhaps last, we cannot forget the poorest. They may not be systemically important, but the people who are suffering the most as always are the poorest and the most vulnerable. So we have to find space in London and space in the global recovery program to extend help to the 1 billion, 1-1/2 billion people for whom it's not just a question of lowering consumption or lowering the living standards a little bit, but it's a question of not being able to send their kids to school, not having sufficient

nutrition which will have effects over decades, and we must not forget that last aspect of the crisis.

MR. ANTHOLIS: Where can we expect that surge of demand and growth in emerging markets to come from? China has stepped forward with a stimulus plan that I think Eswar ranks as moderate or modest. Other developing countries have been more limited in that way after years of us preaching to them for austerity. And the rest of the industrial world other than the United States isn't stepping forward with a stimulus. How does that play out either at this meeting or in the future over the next several months?

SPEAKER: That's why the resources that have to be made available to the development banks and to the IMF are extremely important. The U.S. has called, Mike may want to elaborate on it, on a very strong IMF response, very strong financing from the IMF, liquidity to the emerging markets. Liquidity has been provided to the U.S. financial system, in Europe, in Japan, but the emerging markets don't have the same capacity to do that and the IMF has to help them do that. We cannot let the banks in the emerging markets collapse or the corporate sector, and that's where the IMF's role and the liquidity that has to be given, the resources that have to be given to the IMF, are very important.

One more point. Of course, the governance of the IMF, we'll maybe come back to that, but we cannot have a G-20 with China, India and Brazil at the table and others and think that the IMF can be governed in the old ways.

MR. ANTHOLIS: That's why I was going to turn to Mike on both those points. Are you sensing from some other colleagues that there is that support for the IMF as well as other multilateral and individual aid? We've seen recently that OECD is going to come out with a report saying that while we're doing a little bit better than last year, we're still not at the Gleneagles goals. You've got a G-7 process that you're a part of as well as the G-20 process where these issues are on the table including the reform of governance that marries up to these. What do you see the prospects of these various strands coming together in the next set of conversations?

MR. FROMAN: I think Kemal's point is absolutely right on, which is that key to the overall recovery of demand and key to preventing this crisis from going through another cycle or downward cycle is making sure that as capital is withdrawn from emerging markets and developing countries that the IMF and the World Bank and the other MDBs are there to try and provide that capital, and this is a very different sort of crisis than the crises that the IMF and the MDBs have dealt with in the past. This is

largely with some exceptions a private sector crisis in these countries with corporations who will have difficulty rolling over their foreign exchange liabilities, with trade finance having collapse, and as Kemal said, with the need for bank recapitalization in these countries, but the countries themselves don't necessarily have the wherewithal to provide. So the IMF, the World Bank, the other MDBs need both the resources, but also need appropriate approaches and appropriate facilities to deal with the specific elements of this crisis and that's very much on the agenda there.

In terms of the reform, I think it goes part and parcel with the expansion of their role in this crisis. We will be going to London very much in support of comprehensive reform of governance of the international financial institutions and giving the emerging markets and developing countries -- or having the institutions reflect the realities of the economy now. So I would expect in the near term for those governance issues to be addressed as well.

MR. ANTHOLIS: Protectionism has started coming up as a phrase certainly with the focus on trade protectionism, but also we're starting to hear financial protectionism. Give a sense of how that's playing out in the conversations and how you think it will play out in the meeting.

MR. FROMAN: I think one of the significant accomplishments of the November meeting was this pledge to avoid

protectionism and avoid erecting new barriers to trade and investment. No country has been perfect, but on the whole I think the assessment by the WTO, the World Bank and others is that the steps that have been taken since then have not had a significant deleterious impact on trade and investment. From the President's perspective or from the U.S. perspective, we've had a few issues ourselves and the President has said buy America has to be implemented in a way that's consistent with international trade obligations. He has said that this is not a time to take actions that would further reduce trade when trade has fallen off so much, and that we will be taking actions to rectify barriers as they arise, and I think that's generally the approach of the other countries. Again everybody is a bit of a sinner, but this is a time for everyone to come back and to try a bit of a revival meeting among sinners, and I think there will be a strong message coming out of there.

The second point is actually a bit more difficult because there is the risk not just of trade and investment protectionism but of economic nationalism or financial nationalism more generally. Certainly as each country takes steps to bail out its own banks or its own auto sectors or other sectors there will be a tendency to ensure that that money is spent in ways that benefit the national economy and I think all of us will be coming together to at least exhort each other to try and do this in a way

that minimizes negative and adverse impacts on others. But it's becoming aware of the issue, having institutions monitor what each country is doing and be able to use that monitoring to come back to hold the nations accountable.

MR. ANTHOLIS: Kemal, how are you and folks at the U.N. and particularly the big emerging and developing countries seeing protectionism? Is it a fear just about trade or is it extending to these other areas, and do you expect that to infect other parts of the conversation?

MR. DERVIŞ: I think it is a very important issue. Of course, many of the emerging markets, one of the driving forces of growth has been exports. One of the worrisome parts of this crisis is that any individual country cannot export itself out of the crisis. When I was in the Turkish government, it was an emerging market crisis, one of the things we could do is export a lot more into the world economic. Now unfortunately because the crisis is so global now, exporting yourself out of it by yourself is not an option. So we have to have this global revival of demand and everybody participating in it.

On the financial sector, I do believe there are lots of worries about protectionism and measures that really are not a level playing field in the financial sector. We may not have time in the London meeting to go into the details of that but I think it's something for the agenda in the future

which is very, very important. On the financial sector which is so important let me just add one other point. That is that when you look at financial and banking sector crises in history around the world, sometimes the cost of recapitalization goes all the way to 40 percent of GDP. Let's say in a typical crisis, somewhere between 20 and 40 percent of GDP. It's a huge amount of money, and this is why it's so difficult because these resources are absolutely necessary but politically of course injecting so much money, and I'm not just talking about the U.S. but across the world into the financial sector is a very difficult thing to do. I do believe in the U.S. there is one element which makes it somewhat easier, that there is a lot of private money available and I do believe the President's plan and the Treasury's plan tries to tap that private money to complement the public money and I think that that will make it more feasible rather than just trillions of public money. On the other hand, the way you combine those two and the conditions make it politically of course very tricky.

MR. ANTHOLIS: In the last few minutes that we have here, Mike, and while Kemal is here as well for this part of the conversation, one of the things that's fascinating about these meetings is there's a whole lot of preparation, Sherpas, this, that and the other, and then it's essentially a bunch of leaders getting together. So sort of at a personal level can you give us some insight into how President Obama is thinking about this

meeting, what his own goals vis-à-vis others leaders are, and the same for Secretary General Ban Ki-moon who has been on the stage for about a year or about 2 years now, just how are they personally steering themselves through this course?

MR. FROMAN: I think for President Obama this is an opportunity to show that the U.S. is fully engaged with the rest of the world, and it's also an opportunity for him to show his view of U.S. leadership, which is he'll be going to London, he'll be going to London in part to listen and to understand where other countries are coming from, but he's also going to London to lead. And he goes to London well positioned to lead by example, because if you go down the agenda that we've been talking about this morning whether it's fiscal stimulus, the U.S. economic recovery plan is a very robust example of fiscal stimulus, fixing the financial sector, the various plans that the Treasury has laid out over the last couple of months including just last week, are a critical part of dealing with that problem. On the regulatory reform side, the testimony and speech that Secretary Geithner gave last week beginning to lay out our approach to systemic risk regulation is a key part of this regulatory agenda. So he will be able to go to London and say here is our global agenda, we each need to take steps in the following areas, and the U.S.

has begun to do so and we look forward to talking with the other countries and learning about what their perspective is on this as well.

MR. ANTHOLIS: Kemal?

MR. DERVIŞ: For the Secretary General I think one thing that's very, very important is that he goes in a sense also representing those who are not there. I think the G-20 and however many countries we'll finally have there, 22 or 23, is a great step forward because you really have the big actors, you really have to work together. It's unwieldy. It's a little too large. But having meetings without Brazil, without China, without India, that really doesn't make much sense that I can see. But there are all the others, and at the end of the day the whole world community is terribly affected by this crisis. Africa is affected. The poorest countries are affected. And I think for the Secretary General, his priority is to represent also their views, their vulnerabilities, and to make sure that he plays the role of a bridge if you like between the systemically important countries and the smaller ones. Some of them are not poor, they are small rich countries not represented, but particularly the poorest countries so that they feel that their interests and their voice is heard. I think that is his key mission.

MR. ANTHOLIS: Thank you both so much. Kemal is going to stay and Michael is going to have to leave, but we really appreciate you

taking the time to come over and spend a few minutes with us and give us a sense of what's going on.

MR. FROMAN: My pleasure. Thank you.

MR. ANTHOLIS: Thanks. Great to see you, Mike.

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I, Carleton J. Anderson, III do hereby certify that the forgoing electronic file when originally transmitted was reduced to text at my direction; that said transcript is a true record of the proceedings therein referenced; that I am neither counsel for, related to, nor employed by any of the parties to the action in which these proceedings were taken; and, furthermore, that I am neither a relative or employee of any attorney or counsel employed by the parties hereto, nor financially or otherwise interested in the outcome of this action.

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