



The G20 Leaders Summit: Recovery and New Beginnings

Policy Brief

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Abstract

On April 29, 2010, representatives of the world's leading business associations gathered in the national capital region for the Canadian Chamber of Commerce's G8/20 Business Summit. This important forum, held in advance of the June G8 and G20 Leaders Summits, enabled the business community to play an active role in finding practical solutions to the challenges facing the global economy. Business leaders engaged in discussions and developed a set of recommendations in three major areas: restoring long-term confidence in global markets, supporting trade liberalization and rejecting protectionism, and addressing climate change. The joint G8 business declaration with its recommendations was signed at the event and formally presented to Prime Minister Stephen Harper, who addressed the gathering. In turn, signatories to the declaration pledged to present it to their respective heads of state prior to the forthcoming G8 and G20 summits.

This report reviews the front-and-centre issues that will be discussed at the G20 summit in Toronto on June 26 and 27, 2010, and outlines the key recommendations of the joint business declaration.



G8/20 Business Summit, presented by the Canadian Chamber of Commerce, April 29, 2010

The Canadian Chamber is committed to fostering a strong, competitive and profitable economic environment that benefits all Canadians. This paper is one of a series of independent research reports covering key public policy issues facing Canada today.

We hope this analysis will raise public understanding and help decision-makers make informed choices. The papers are not designed to recommend specific policy solutions, but to stimulate public discussion and debate about the nation's challenges.

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Introduction

The Group of Twenty (G20)¹ industrialized and emerging-market countries delivered unprecedented, swift and coordinated measures to pull the global economy from the brink of collapse and stabilize the world's financial system. The G20's success and spirit of collaboration have made it the premier forum for international economic cooperation. Now, it will be judged by whether it can nurture economic recovery and lay the foundation for sustainable and balanced growth.

When the G20 leaders meet in Toronto on June 26 and 27, they are expected to tackle an ambitious agenda that includes: mapping out a strategy for countries to withdraw enormous economic stimulus, finding a way forward on resolving

global imbalances, pressing for an open and rules-based trading regime, and strengthening the global financial regulatory system.

The summit is an opportunity for Canadian leadership. Canada stands proud on the world stage through its actions and example. Amidst global financial turbulence, our banking sector was recognized as the world's soundest, thanks in good part to strong regulation and supervision. Canada has the best fiscal position among major industrialized countries. As other nations erected walls, Canada rejected protectionism and embraced trade liberalization. Our success provides political capital we can expend to influence reforms and present solutions on a spectrum of global issues.

Exit strategies

The G20 countries committed \$5 trillion in fiscal stimulus by the end of 2010 to revive the global economy. They must now formulate well-timed strategies to wean economies off this massive injection. Sustained growth hinges on the private sector resuming its role as the primary driver of economic growth. The timing and pace at which governments can withdraw stimulus will depend on the strength of the economic recovery in each country.

Many advanced economies emerged from the recession with the highest deficit- and debt-to-GDP ratios since the Second World War. The International Monetary Fund (IMF) estimates the average deficit among advanced G20 economies will reach 8.7 per cent of GDP in 2010, well above the pre-crisis (2007) level of 1.9 per cent. The IMF projects that, in 2014, government debt in advanced G20 economies will hit 118.4 per cent of GDP, on average, compared with a pre-crisis level of 78.2 per cent.²

Large deficits are not sustainable for long, especially when nervous markets drive up the cost of servicing the growing debt. The crisis in Greece has made clear the peril of public finances that have spun out of control.

Keeping the confidence of financial markets requires governments to develop and communicate clear, credible plans for significantly reducing their deficits over the medium term. Difficult decisions will need to be made. Cutting spending, improving the efficiency of government programs and services and embracing public-private partnerships are necessary to ensure longer-term fiscal sustainability. The ability of businesses to create jobs and innovate would be severely shackled by increasing taxes.

¹ The G20 consists of nine industrialized countries (Australia, Canada, France, Germany, Italy, Japan, Russia, the United States and the United Kingdom), the EU, which is represented by its rotating president, and 10 emerging-market economies (Argentina, Brazil, China, India, Indonesia, Korea, Mexico, Saudi Arabia, South Africa and Turkey). Collectively, the G20 economies account for 90 per cent of the world's GDP, 80 per cent of world trade flows (including EU intra-trade) and two-thirds of the world's population.

² Horton, Mark, and Philip Gerson (2009). "The State of Public Finances Cross-Country Fiscal Monitor: November 2009." *IMF Staff Position Note*. Washington: International Monetary Fund. November 3.

Addressing global imbalances

The G20 will also have to deal with global imbalances in trade and capital flows, the most visible being the large and persistent current account deficit in the United States mirrored by sizeable current account surpluses elsewhere, notably in rapidly growing East Asian economies and oil-producing countries. These imbalances

pose a risk to global economic and financial stability. They must be addressed with policies aimed at achieving fiscal consolidation in advanced countries and an increase in domestic consumption and real exchange rate adjustments in countries with large current account surpluses.

Resisting protectionism and promoting global trade and investment



The G20 leaders must embrace an effective and efficient rules-based trading system and champion unencumbered global commerce. They must reaffirm their commitment to open markets through new multilateral, regional and bilateral free trade and foreign investment agreements and remove existing barriers to trade and capital flows. They must set an example by quickly removing protectionist measures adopted during the downturn, including barriers contained in stimulus packages.

According to the Global Trade Alert, 220 beggar-thy-neighbour policies were imposed by G20 countries between November 2008 and January 2010. Another 38 measures were implemented that are likely to have harmed some foreign commercial interests.³

It is alarming that as of January 2010, there were 198 suspicious protectionist measures in the pipeline—publicly announced but yet to be implemented—by world governments.⁴

The impulse for protectionism may be understandable when governments want to show they are doing everything possible to preserve their

³ Evenett, Simon J. (ed) (2010). *Will Stabilisation Limit Protectionism? The 4th Global Trade Alert Report*. London: Centre for Economic Policy Research. February 15.

⁴ Ibid.

citizens' businesses and jobs; however, beggar-thy-neighbour policies threaten to derail recovery, drag down future growth and reduce income potential for everyone. They inflict the greatest damage on the world's most vulnerable.

The stakes for Canada are high. When so much of our prosperity depends upon trade, protectionism can have a devastating impact on communities throughout the country.

Canada provides an example the rest of the world should emulate. Canada has taken significant steps to open markets and keep them open. The 2010 federal budget eliminated all remaining tariffs on manufacturing inputs and machinery and equipment, making Canada the first tariff-free zone for manufacturers in the G20. Canada recently negotiated a number of bilateral trade and investment agreements. In April 2010, it concluded third-round free trade negotiations with the European Union. The proposed Comprehensive Economic and Trade Agreement (CETA), the most ambitious since NAFTA, could generate C\$40 billion in annual bilateral trade and investment by 2014.⁵ Canada and India are making good progress in scoping the content of a Comprehensive Economic Partnership Agreement (CEPA) and Canada is negotiating high-standard Foreign Investment Promotion and Protection Agreements (FIPAs) with China and India. These initiatives are sending a resounding message to the rest of the world that, instead of turning inwards, Canada has a confident view of the role it can play in the global economy. It demonstrates both to the world and to Canadians that our country is looking beyond the recession with an eye on creating greater future prosperity.

According to the United Nations Conference on Trade and Development (UNCTAD), "after almost two decades of nearly unequivocal support for investment liberalization, many countries have started to re-evaluate these policies, and some have introduced adjustment, thereby exercising

their right to regulate foreign investment to pursue domestic policy objectives. One of the main areas where a more restrictive approach towards foreign investment has become manifest relates to national security and to the protection of strategic industries and critical infrastructure."⁶ UNCTAD warned that, if the defence of so-called "strategic industries" becomes more widespread, it "could have severe effects on economic growth, hinder an optimal resource allocation and result in significant investment distortion."⁷

The G20 countries must set an example by not raising existing barriers or imposing new ones on outward and inbound investment. The criteria for blocking foreign investment in the defence of "national security" or of a "strategic industry" should be narrowly defined and only applied under exceptional circumstances. At the same time, all international agreements must include high standards of investment protection, including non-discrimination, national treatment and fair and equitable treatment. The agreements must afford prompt and adequate appeal mechanisms, effective compensation in the event of discrimination or expropriation and access to international arbitration to resolve disputes.

Additionally, it is vital to Canada's economic prosperity that national borders do not impede the safe and efficient flow of goods and travellers. The strong link between security and trade must be recognized and a proper balance must be struck.

The G20 leaders must coordinate efforts to combat illicit activities like counterfeiting, trademark infringement and piracy. The OECD estimates that international trade in counterfeit and pirated goods was worth up to US\$250 billion in 2007.⁸ Leaders must give particular attention to enforcing the World Trade Organization (WTO) Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) and advancing negotiations on the Anti-Counterfeiting Trade Agreement (ACTA).

⁵ The European Commission and the Government of Canada (2008). "Assessing the Costs and Benefits of a Closer EU-Canada Economic Partnership." Ottawa: Foreign Affairs and International Trade Canada. October. The joint study indicated that liberalization of trade in goods and services has the potential to give a \$12 billion annual boost to the Canadian economy.

⁶ The United Nations Conference on Trade and Development (2009). *The Protection of National Security in IIAs*. New York and Geneva: United Nations. August 1.

⁷ Ibid.

⁸ Organisation for Economic Co-Operation and Development (2009). "Magnitude of Counterfeiting and Piracy of Tangible Products: An Update." Paris: OECD. November.

Finally, now is the time to complete the WTO's Doha Round of multilateral trade negotiations. With a concerted push by the G20 leaders, WTO countries can put together an ambitious and balanced package that helps both developed and developing countries. New political energy must be injected to bridge gaps and ensure the final agreement generates new trade flows, reduces the cost of doing business across national borders and increases predictability for companies.

The Washington-based Peterson Institute for International Economics estimates that a successful conclusion of the Doha Round could increase world output by US\$165 to \$283 billion annually. Agriculture and non-agricultural trade liberalization could boost global GDP by \$63

billion a year. Canada's export-oriented farmers and manufacturers have much to gain. Sector-specific agreements in chemicals, electronics/electrical goods and environmental goods offer the possibility of even greater global access for Canadian businesses and could increase global GDP by an additional \$56 billion per year. Meaningful liberalization of services could raise world GDP by \$46 billion annually and further expose Canada's services sector to international markets. Trade facilitation improvements, including reforming customs procedures, slashing red tape, reducing transaction costs for imports and exports of goods and services, and publications standards could expand global output by roughly \$118 billion per year.⁹

Financial regulatory reform

Financial regulatory reform has remained at centre stage with good reason. Richard Fisher, president and CEO of the Federal Reserve Bank of Dallas, wrote, "In an economy, the central bank is the heart, money is the lifeblood and financial markets are the arteries and capillaries that provide critical sustenance to the muscles—the makers of goods and services and creators of employment. A properly functioning cardiovascular system fosters healthy growth; if that system fails, the muscles atrophy and the body breaks down."¹⁰

A well-functioning financial system is critical for economies to realize their full potential. Entrepreneurs must tap financial capital to transform their ideas into a successful venture. Businesses require capital to expand and modernize their plants and equipment. Families rely on lending institutions to finance their homes and their children's education.

In April 2009, the Brookings Institution published "Know Thy Neighbor: What Canada Can Tell Us About Financial Regulation."¹¹ The article notes,

"The Canadian banking system has long been regarded by the IMF as a paragon of international best practices. The World Economic Forum recently ranked it the soundest in the world. And it looks better with every passing day. As during the Great Depression, when only a few inconsequential banks failed in Canada, the overall system has remained solvent and solid amid the current global crisis." The Institution concluded: "Clearly, there is something to be said for studying Canada's more centralized, and apparently better-coordinated, regulatory bodies."

Without a doubt, Canada has credibility and will bring to the table a unique and important perspective on financial reform. As part of an international financial reform agenda, priority should be given to ensuring adequate capital and liquidity standards and to building a principles-based framework for global financial supervision through better collaboration and coordination among regulators. Achieving a commitment to ambitious peer review will be an important milestone.

⁹ Hufbauer, Gary C., Jeffrey J. Schott, and Woan Foong Wong (2010). "Figuring Out the Doha Round." *Op-ed in Vox-EU.org*. Washington: Peterson Institute for International Economics. February 22.

¹⁰ Fisher, Richard W. (2010). "Reflections on the Financial Crisis: Where Do We Go From Here?" *2009 Annual Report*. Dallas: Federal Reserve Bank of Dallas. April 26.

¹¹ Nivola, Pietro S., and John C. Courtney (2009). "Know Thy Neighbor: What Canada Can Tell Us About Financial Regulation." Washington: The Brookings Institution. April 23.

As Bank of Canada Governor Mark Carney has stated, “The financial system will be more stable if market infrastructure is substantially improved, products are more standardized and transparent, and banks are adequately capitalized to fulfill their market-making and credit intermediation roles.”¹² Mr. Carney added that the ultimate goal of financial sector reform is to make each financial institution and the financial system as a whole, more resilient.

Policymakers must assess all regulatory proposals to determine their impact on availability of credit/financing. It is not sufficient to analyze each regulation in isolation. Policymakers must also consider the cumulative impact of proposed regulations.

In the end, new standards for banking regulation and supervision must be sufficiently strong and responsive to avoid another financial crisis, while still encouraging growth and financial innovation. In the words of U.S. Federal Reserve Chairman Ben Bernanke, “When proposing or implementing regulation, we must seek to preserve the benefits of financial innovation even as we address the risks that may accompany that innovation.”¹³ Policymakers, he added, should work to devise “principles-based policy responses that can be applied consistently across the financial sector to meet clearly defined objectives.”¹⁴

A proposal being discussed in advance of the G20 summit is a global tax on financial institutions’ liabilities (except insured deposits and equity) or on profits and remuneration to cover the cost of any future bailouts. Canada is rightfully opposed to the idea first and foremost because there were no taxpayer bailouts of financial institutions in Canada. Additionally, a tax levy would remove capital from financial institutions, lessening their ability to absorb losses. It could trigger more risk-taking because of the perception financial institutions will be bailed out, much as the too big to fail mentality gives banks a potentially dangerous incentive to get bigger and riskier because they are nestled under implicit guarantees they will be bailed out by the taxpayer.

Another idea making the rounds is a global tax on financial transactions. In the early 1970s, Nobel laureate James Tobin had proposed a supra-national tax on foreign exchange transactions to discourage short-term trading and excessive speculation. Now, a much broader tax on global financial transactions (such as currency, bonds, equities and derivative trades) is being proposed to generate revenue to cover the cost of any future bank bailouts. Such a tax would lower market liquidity and seriously harm investment and economic growth. European Central Bank Governing Council member Christian Noyer stressed, “We absolutely have to avoid situations in which the payment of taxes or levies is understood as a *de facto* bailout policy insurance.”¹⁵

12 Remarks by Bank of Canada Governor Mark Carney, “Reforming the Global Financial System,” at a Rendez-vous avec l’Autorité des marchés financiers. Montréal: October 26, 2009.

13 Remarks by U.S. Federal Reserve Chairman Ben S. Bernanke, “Regulation and Financial Innovation,” to the Federal Reserve Bank of Atlanta’s 2007 Financial Markets Conference. Sea Island, Georgia: May 15, 2007.

14 Ibid.

15 Remarks by Banque de France Governor Christian Noyer, “Banking Regulation and the Financing of the Economy,” to the Paris-Europlace Forum. New York: April 26, 2010.

Post-Copenhagen: action on climate change

Climate change is not a focus of the G20 discussions; however, it is too important an issue to ignore. While the United Nations Framework Convention on Climate Change (UNFCCC) has been the primary forum for these discussions, the G20 can play an important role in bringing the largest economies together to advance an agreement leading to a low carbon economy.

Building on the Copenhagen Accord, and taken note at the 15th session of the Conference of the Parties to the UN Framework Convention on Climate Change (COP15), the agreement must include all major greenhouse gas (GHG) emitters with binding reduction commitments that establish a level playing field. Both the private and public sectors share the responsibility to act, with advanced economies working with emerging-market nations, to achieve balanced and sustainable economic growth. Since many developing countries are struggling to provide even the most basic necessities to their citizens, a global approach to addressing climate change will require innovative financing mechanisms to ensure their participation. An effective compliance system must be developed to enable measurable, transparent and verifiable comparisons of the climate change efforts among countries.

Many businesses are meeting or exceeding regulatory requirements and are investing in research and technology to reduce their environmental

footprints. They recognize that addressing environmental issues is good business.

An effective program to reduce GHG emissions hinges on a range of factors, including the speed of developing, commercializing and deploying low- and near-net-zero carbon energy technologies and technologies that increase end-use energy efficiency. Some advanced technologies may not be sufficiently attractive to penetrate the market on a large scale without supporting policies or incentives. Other technologies, like those that capture or sequester carbon dioxide (CO₂), are still in the early stages of development.

Ultimately, no single technology will meet the challenge by itself. Significant investment in research and development (R&D) is required to develop a portfolio of advanced technologies. Since many technologies will take decades to move from R&D to widespread implementation, governments must commit to programs that support new technology development by the private sector.

Climate change and energy security policies must be mutually reinforcing. Increasing energy efficiency, diversifying the mix of energy sources and eliminating wasteful energy subsidies are vital for any future climate change strategy.



Conclusion

As a small, open and export-dependent economy, Canada has a vested interest in ensuring a well-functioning global governance architecture that promotes stable and sustainable economic growth, a sound financial system and open and transparent trade and investment policies. The G20 summit in Toronto gives Prime Minister Harper an opportunity to promote Canadian values and present solutions that serve our own interests and the global community's in a balanced way. The prime minister must call on world leaders to not simply talk about their opposition to protectionism, but to demonstrate it in their actions. He should make it clear that Canada is prepared to match its deeds to its principles, both in the Doha negotiations and in dismantling barriers here at home. Prime Minister Harper must urge world leaders to emulate Canadian financial system practices and regulations.

Although Canada is but one voice, and a relatively small one at that, this is an opportunity for Canada to have an impact far greater than what the size of its population or its economy would suggest.

We must seize the moment.



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