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The G20: The Last Defence of Multilateralism?

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Participants listening to the opening address by Indonesian President Joko Widodo (on-screen) during the opening of the G20 finance ministers' meeting in Jakarta on February 17, 2022. Picture; BAY ISMOYO/POOL/AFP.

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EXECUTIVE SUMMARY

- The G20 Summit was created to garner political support and commitment to coordinate monetary and fiscal policies, address global economic challenges, and deliver global public goods, which are goods whose benefits affect all citizens of the world.

- But, the G20 Summit has shown signs of withering partly because it has traded off its focus on 'inclusivity'. It now consists of stupefyingly confounding auxiliaries (T20, B20, etc.) and ever-growing mandates. Meanwhile, it sweeps under the rug some of the more difficult, politically sensitive commitments and reforms, including those on financial regulations, the international monetary system, and governance of international financial institutions. When put to the test, such as at the start of the COVID-19 pandemic, the G20 failed to step up decisively. Moreover, this year is not the first time the G20 looks more like an arena for power tussles than an international economic forum.

- The G20's effectiveness can be revived if it prunes itself massively, in substance and organization, while keeping its core elements and focus such as monetary and fiscal policy coordination, as well as financial regulatory reforms. Most importantly, the G20 must rise above geopolitical conflicts among its member countries. If increasing geopolitical power infighting continues to plague the G20, its promise to manage the global economic crisis and deliver global public goods the world needs so badly, will remain pie in the sky.

- After the Indonesian Presidency, the next two G20 Presidencies – India and Brazil – like Indonesia, could use political and economic diplomacy as 'middle-power' countries to help pull the crumbling G20 away from the increasing geopolitical tensions existing between its big-power members.

INTRODUCTION

The zero-sum paradigm – a paradigm that the progress of some stymies the progress of others – is seemingly becoming more entrenched in an increasingly multipolar world. This notion, often adopted in the military and security fields, has exacerbated the security dilemma[1] and transcended a whole gamut of economic areas. It cripples our ability to build global economic cooperation that is so much needed for addressing the multi-sided global economic crises and global public good crises the world is facing today. Indonesia's G20 Presidency's theme, 'Recover Stronger, Recover Together', echoes the cooperative, positive-sum paradigm on which the G20 was founded. But increasing geopolitical tensions might render the G20 ineffective in delivering its goal.

The G20 and its Leaders Summit were initiated in 1999 and 2008 respectively against the backdrop of world economic crises. By 2009, the G20 Summit was recognized as the premier forum for international economic cooperation to coordinate monetary and fiscal policies as well as address major strategic issues related to the global economy. Its leverage to the leaders' level, involving not only major economic powers but also emerging and developing economies, shows that the G20 is expected to deal with extraordinary and strategic global economic issues that have global spillovers and that affect the global population. Since the G20 Summit is held at the leaders' level, the G20 gives opportunities to garner political support and commitment on politically sensitive issues that need commitment and coordination at the highest level.

The G20 was a (belated) recognition of not only the shifting of economic power to emerging economies and developing countries, but also the need for more and better global public goods, i.e., goods whose benefits affect all citizens of the world. These include internationally agreed rules to standardize and stabilize the financial markets, or to avert cross-border tax evasion. A rule-based multilateral system is needed for an increasingly convoluted global economy, which is now increasingly interlinked by digital technologies, and not just by global trade, global value chains, or international capital flows.[2] In fact, since the Global Financial Crisis 2008-9, world trade over world GDP, international global value chains over world trade, and international capital flows (foreign direct investment and portfolio investment) as share of world GDP have either stagnated or declined.[3] A rule-based multilateral system is also key for smaller countries to function, flourish and prosper since a rule-based multilateral system gives these countries standards, certainty and protection against possible erratic and detrimental behaviours from big-power countries.

The concerted policy actions born out of the G20 Summit during the Global Financial Crisis 2008-9, especially the 2009 commitment to concertedly inject US$5 trillion worth of fiscal stimulus into the global economy to keep and create jobs, were successful in staving off the global economic depression. Once a highly influential and regarded forum, G20's solidarity may have waned because of the increasing geopolitical tensions while its ever-growing mandates and auxiliaries stupefy its ability to focus, stifling G20's effectiveness to manage global economic crises and deliver global public goods.

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WITHERED SOLIDARITY AND LOST FOCUS?

The G20 has many achievements, the most recent being the ground-breaking OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting to tax global corporations, including big tech giants, a minimum of 15%, and to redistribute 25% of the largest companies' residual profits to market jurisdictions. At the same time, however, there is evidence of 'withering' in the international forum.

First, it has lost focus. The G20 is becoming like a Christmas tree with an ever-expanding mandate, discussing everything under the sun, with each rotating presidency being keen to leave a legacy. The G20 has also become an alphabet soup with confounding G20 auxiliaries, for example, B20 for business, T20 for think tanks, and C20 for civil society. Although the causality of the G20 losing focus and getting 'obese' can go both ways, its ever-growing mandates and auxiliaries can be partly blamed on its rotating presidency. For example, Civil20 Summit was first introduced by Russia's G20 Presidency in 2013 while South Korea's G20 Presidency in 2010 added the development agenda and Mexico's G20 Presidency threw in the food security agenda. Some of these agendas were multi-year action plans meant to be carried over to later presidencies.

Unfortunately, there is a trade-off between being inclusive and being focused.

Moreover, some critical financial regulatory reforms achieved in the early G20 summits, such as the 2010 Dodd-Frank law, were also reversed although that reversal was more of a national choice during the Trump administration than anything else.[4] Political commitments on trade openness by the G20 leaders, which are needed especially in the face of a failing WTO, have not been strong enough to ward off increasing protectionist sentiments (even among G20 members), especially at the heights of the COVID-19 pandemic, and in the face of declining global trade as share of global GDP since the Global Financial Crisis 2008-9.[5]

Meanwhile, the G20 sweeps under the rug some of the more difficult, politically sensitive reform commitments, including those on financial regulations (especially in regulating non-bank financial intermediaries), the international monetary system, and international financial institutions (IFIs) governance reforms.

As an example, as reiterated at the G20 London Leaders Declaration in 2009[6] that 'the heads and senior leadership of the IFIs should be appointed by using an open, transparent, and merit-based selection, not based on nationality, leaders of some IFIs are still political appointees of the largest-shareholding countries in the institutions. Non-borrowing member countries still hold the majority of votes in some IFIs, leaving little space for emerging economies and developing countries in the global economic order (see also Basu, 2002).[7] [8] Although most decisions such as loan approvals are based on a simple majority rule, the United States remains the *only* member country of the IMF[9] and the World Bank[10] with veto power over major decisions such as organisational structural changes that need a supermajority vote (85%), putting the multilateralism spirit into question. But, IFIs reforms need to go beyond voice and quota reforms. The US Secretary of the Treasury, Janet Yellen, recently asserted the need for a major reboot in IFIs mandates[11] for better capability in the delivery of global public goods.

Second, when put to the test, such as at the start of the COVID-19 pandemic, the G20 failed to step up decisively. While the economic crisis caused by the Covid-19 public health crisis was deeper and more widespread than that of the Global Financial Crisis 2008-9, the G20 has disappointed many ardent and articulate academics and observers.[12] A public health crisis constitutes a positive-sum game where "no one is safe until everybody is safe", but when medical supplies and vaccines were in short supply, countries reverted to a zero-sum game. Countries, including G20 members like the EU, reversed globalization by banning exports of medical supplies and decoupling supply chains.[13] In December 2020, South Africa and India called for the WTO to suspend Intellectual Property Rights related to COVID-19 vaccines and medicines to control the pandemic but it was rejected by some high-income countries, including the US, UK, and EU.[14] All these countries are G20 members. In its extraordinary G20 leaders' meeting held on March 26, 2020, G20 leaders were committed to injecting the same US$5 trillion into the global economy as it did during the Global Financial Crisis 2008-9 despite the growth of the global economy since 2009 (which means a lower share of support out of the global GDP), the deeper and more widespread economic crisis the world was facing, and the more dire threat to human lives the COVID-19 pandemic entailed.[15]

Third, power fighting transcends economic rationales. This year is not the first time the G20 looks more like an arena for power tussles than a forum for international economic cooperation. In 2011, the G20 was overshadowed by geopolitical division over the authorization of military strikes to enforce the no-fly zone in Libya. The walk-out of the US Secretary of Treasury and other Finance Ministers in the second Finance Ministers and Central Bank Governors Meeting this year dimmed the prospect of having a meaningful discussion among the world's largest economies to manage global challenges.

More than ten years after the G20 Summit started, we are entering into a more divided, more bifurcated world than was the case in 2008. We are seeing an erosion – not strengthening – of the international, rule-based order since 2008. However, the world cannot afford to make a meal out of it.

GLOBAL ECONOMIC AND GLOBAL PUBLIC GOODS CRISES

First, the international monetary system needs some rethinking. It is dominated by the US dollar as the global currency, but the US dollar is also being 'weaponized' through the use of sanctions.[16] The US dollar as the global currency is no longer neutral nor sustainable as originally intended.[17] The system was initially set up after the Second World War to provide the world with an efficient and neutral payment system. However, sanctions on Russia and Iran in the past clearly belie its lofty aspirations.[18] The system was not set up for an increasingly multipolar world.

For the US itself, its status as the world's reserve currency is subject to national debate as to whether it is desirable and sustainable. There is a strategic leverage but there are also economic costs. It supplies the world with dollars, even if it could mean reducing the competitiveness of its own domestic economy. The Federal Reserve must also take foreign markets into account when making decisions. Although there is no immediate alternative to the US dollar as a global currency on the horizon, the 'weaponization' of the US dollar could increase the use of digital currencies and the creation and expansion of non-dollar-based payment systems such as the BRICS' de-dollarization initiative.[19] [20] However, digital currencies are very volatile with differing rules regulating the sector across the world, while a bifurcated financial services system will stifle business efficiency. The G20 is the forum to discuss reform of the international monetary system.

Second, the Russian-Ukrainian conflict exacerbates the already dire global condition. As both countries are major producers and exporters of natural gas, fertilizers (ammonia, urea, process phosphate) and wheat, the conflict has caused a massive increase in food and energy prices across the world. This shock is made worse with the uptick in demand due to the ongoing recovery from the pandemic and more recently, with major food producers and exporters such as Indonesia and India temporarily banning exports of food commodities including palm oil in the case of Indonesia and wheat in the case of India, due to rising food inflation at home. The result is the return of the "thought-to-be-extinct" stagflation (see Figure 1). Central bankers are taken aback as they know monetary policy cannot solve supply side problems[21] and there is no conventional solution to manage stagflationary shocks. For many economies, central banks are also faced with a dilemma: either to increase interest rates to slow down inflation but risk a full-blown global debt crisis and recession, or to not increase rates and risk hyperinflation. On the other hand, the Russia-Ukraine war is also stifling global economic growth this year, with the forecast being lowered by 1.3 percentage points since October 2021 by the IMF.[22]

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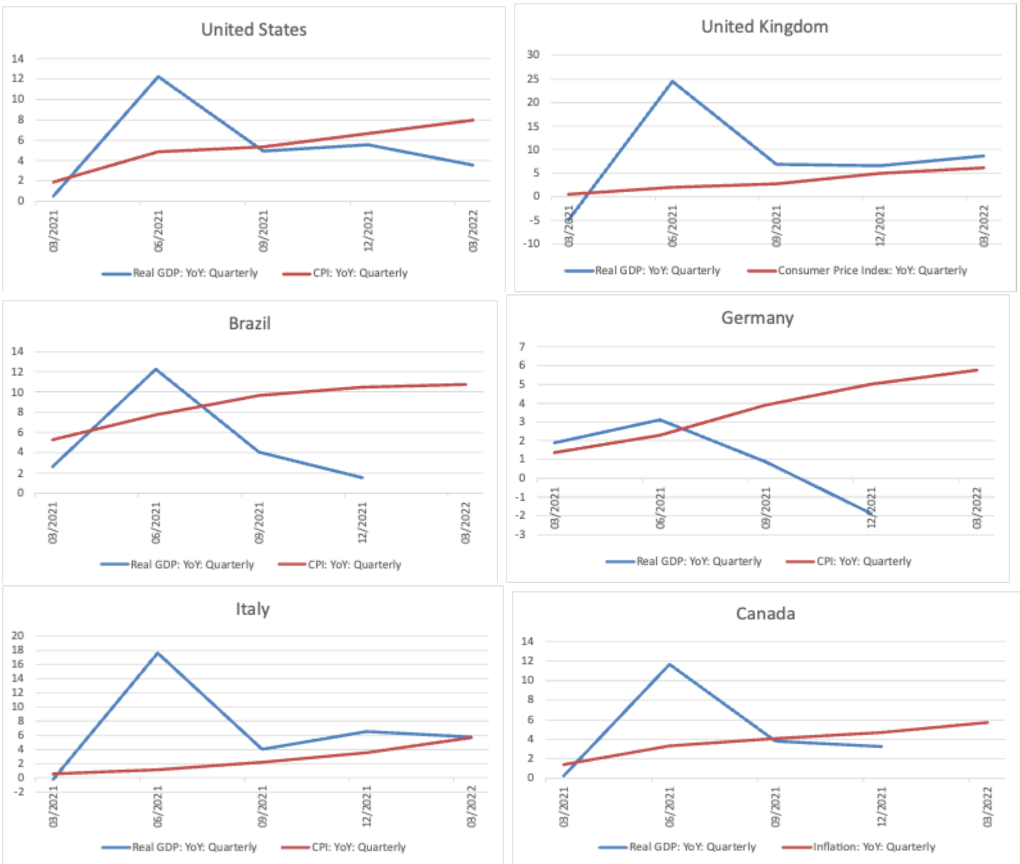
Figure 1: Stagflationary shocks - declining growth and increasing inflation – rippling across the world and crippling the world economy
(Real GDP and Consumer Price Index, Year-on-Year % change, Quarterly)



Source: CEIC and authors' calculations

Recently there has been a push to restructure debts of developing and least developed economies (LDCs) and to figure out the "sustainable" level of sovereign debt of developed economies. Around 60% of low-income countries are now in or at high risk of debt distress.[23] When an economy is close to the zero lower bound on its nominal interest rate (so that it is not possible to use monetary policy to stimulate growth by further lowering the interest rate), it is still possible for a country to sustainably finance a level of government debt that is substantial enough to overcome weak demand in the economy. But, this so-called fiscal 'free lunch' is possible only if the nominal interest rate on debt is below the GDP growth rate.[24] However, with rising interest rates increasing the cost of borrowing, and slowing GDP growth rates, the current global economic environment may not allow for this to continue (see Figure 2). In other words, the only way out may be through fiscal austerity.

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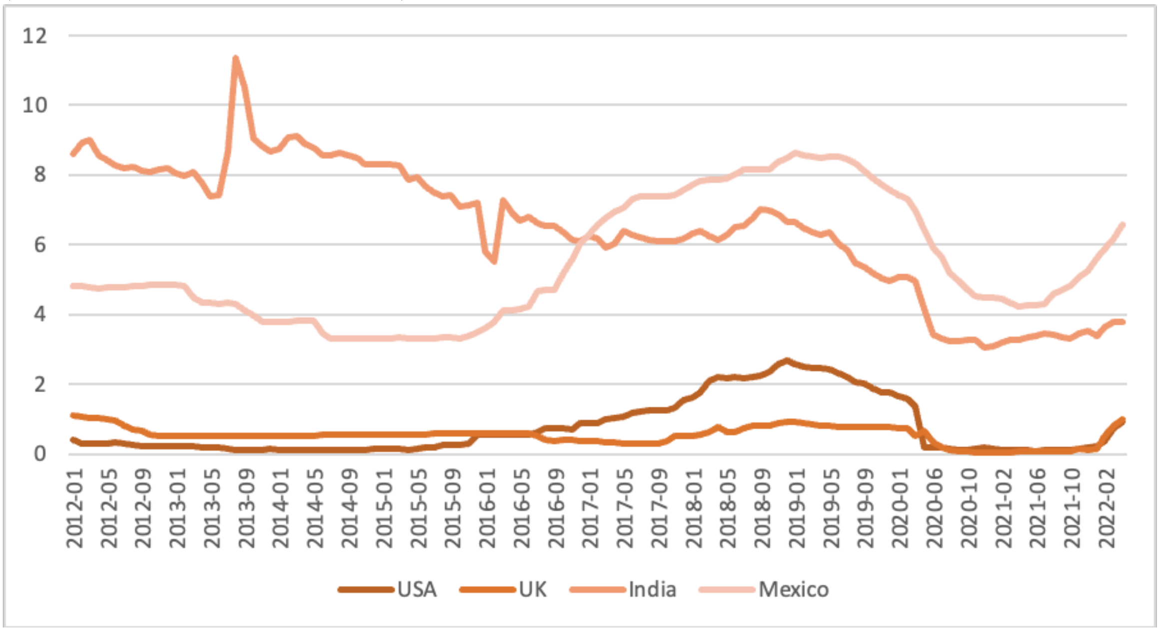
Figure 2: Resurgence of short-term interest rate hikes across the world in Q1 2022
(*Short-term interest rates, in %*)



Source: OECD, 2022

But even this may not work as the global economy is not yet out of the woods from the COVID-19 pandemic. As history has taught us (e.g. the European debt crisis in 2009, or the Asian Financial Crisis in 1997-8), austerity during a recovery or crisis will only worsen the situation. Simply put, there are not enough fiscal and monetary policy instruments to solve the multi-sided economic issues many countries are facing today. In addition, debt re-structurization for developing and LDCs will largely depend on China (see Figure 3), a G20 member, which has not yet committed on any debt forgiveness or restructuring.[25]

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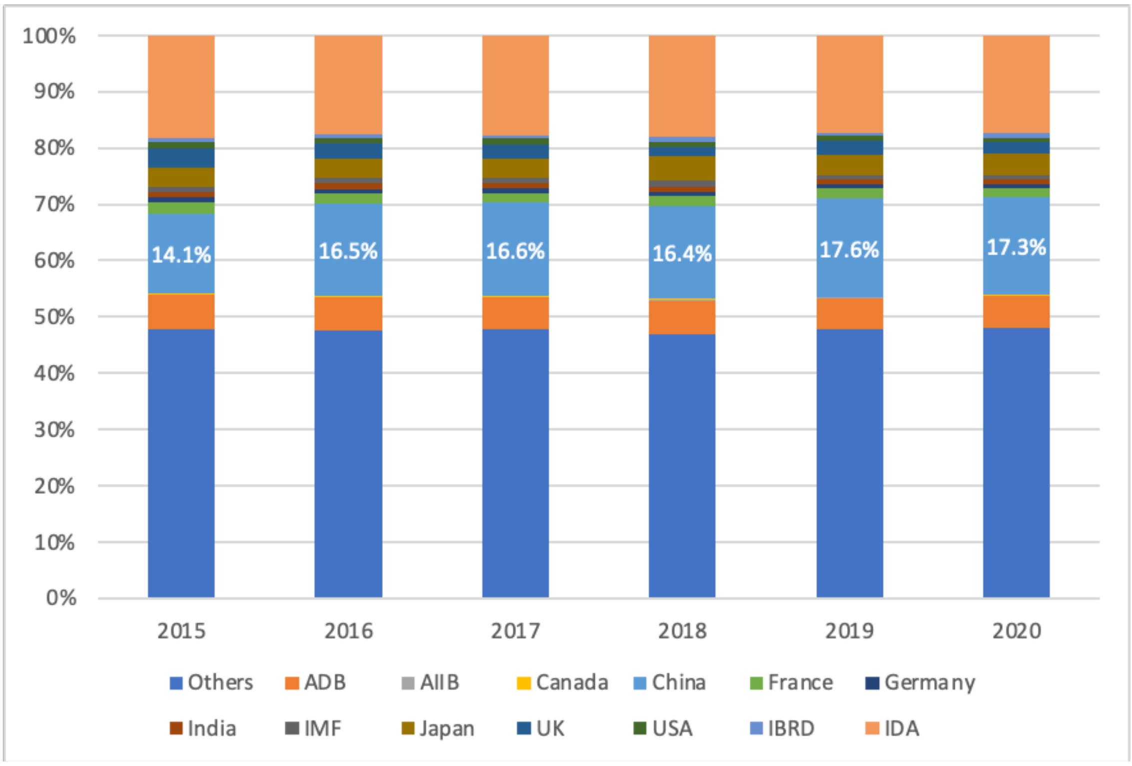
Figure 3: China is the largest single creditor country to developing and less developed countries and its share is increasing
(Total external debt stocks, by creditor, % share)



Source: International Debt Statistics, authors' calculations
Note: Figure only includes external debt stocks for borrowing countries in the G20 Debt Service Suspension Initiative

Again, coordination of fiscal and monetary policies to manage multi-sided economic shocks is something that could be best achieved at the G20 level.

WHAT THE G20 CAN DELIVER

The G20 was in the first place established to coordinate monetary and fiscal policies, and manage world economic crises with global spillovers. To be effective, it needs a lot of pruning, both in terms of substance, and organization-wise. The G20 Leaders Declaration should not consist of 61 articles like that of the G20 Rome Leaders' Declaration in 2021, but perhaps less than 20 articles which are more detailed and binding, rather than being full of rhetoric. The G20 might want to transition back to its pre-G20 Summit's leaner structure by focusing on fiscal, monetary and financial policy coordination, with a few exceptions being extraordinary and strategic global economic issues with potential global spillovers.

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The core G20 mandate must be continued. First, in the immediate term, the G20 could continue to coordinate possible 'unconventional' fiscal and monetary policies that countries around the world might take to respond to global stagflationary shocks, or any other economic shocks and crises in the future. In the same context, this could help accelerate the re-structurization of burgeoning sovereign debts especially among LDCs, under the G20 Debt Service Suspension Initiative. In particular, it could help convince China, as the world's largest creditor, to step up its debt restructuring process.

Second, in the medium term, the G20 could complete its commitment of the G20 financial regulatory reforms agreed upon after the Global Financial Crisis 2008-09, especially with regard to non-bank financial intermediaries.

Third, in the long term, it could help reform the international monetary system and international financial institutions. The transition from the British Pound to the Dollar as the international reserve currency was cemented through the Bretton Woods Agreement in 1944, pushed by the dominant superpower and economic position of the US and its deep and liquid financial system at that time. The US was also the only country without any capital controls after the Second World War. Today, the world needs a more stable and neutral international monetary system with perhaps a supernational currency, such as the SDR.[26] However, without IMF quota reform, the prospect of the IMF turning into a quasi-central bank for issuing a supernational currency and eroding the US's privilege of printing the global currency is dim.

CONCLUSION

The world has been in a global public goods crisis. Multilateralism is failing to deliver them. The world of the future will not be one of pure altruism where all countries altruistically invest in global public goods. Nor will it be a world where all countries resort to national interests and abandon the idea of multilateralism and global cooperative spirits altogether. It will place itself between national interests and multilateralism.

To ensure its existence, the G20 could step back, consider pruning itself, and focus on global economic policy coordination, just as it used to be prior to the G20 Summit in 2008 and in the early years of the G20 Summit. Perhaps, most importantly, it must rise above geopolitical conflicts among its member countries. A leaders' forum like the G20 needs a level-headed conversation to reach commitments on politically difficult issues, but today, leaders have allowed issues to be conflated together. The G20 member countries should be reminded that it is their privilege and responsibility in the exclusive 'G20 club' to be representing the world and should not use it to only advance their national interests. Instead, they should be thinking about how to make their contribution to global issues, even if it comes at some costs to their national interest.

With increasing geopolitical tension among big-power countries who are members of the G20, middle-power countries and emerging economies – who happen to be hosting and

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will be hosting the next two G20 Summits, namely India and Brazil - could use its political and economic diplomacy to steer the forum in this direction. If they fail, any hope that the G20 can meaningfully contribute to the global public goods and the global economy will remain pie in the sky.

ENDNOTES

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[24] See the Goldilocks theory of debt

[25] Shalal and Lawder (2022)

[26] Sheng and Geng (2022)

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