

Perspectives on the London Summit

April 2009



Introduction – looking at London



Since the world's credit markets seized up in the summer of 2007, the financial crisis has generated a long list of superlatives: deepest, worst, costliest. Some of these descriptions have proved accurate, while others have been commentators' exaggerations.

It is fair to say, however, that the G-20 London Summit was the most eagerly anticipated meeting of its kind for decades. The leaders of the world's largest economies set themselves a challenging agenda: agree how to stabilize markets, strengthen the global economic and financial system and put the economy back on track. Leading up to the Summit, the list of questions was long. Could transatlantic disagreements over stimulus packages be solved? Would decisions be influenced by the need for global cooperation or driven by national politics? Did the global economic engine need more oil, or did the world need a new and better engine?

In the end, the Summit achieved what many thought was its most important, if unstated, goal – to present a unified front among governments and boost confidence in the global economy. The details – more than US\$1 trillion for the International Monetary Fund, or the creation of the Financial Stability Board – were, in this view, less important than the pledge to work together to tackle shared problems.

While it will take time to fully understand the Summit's impact, the analysis can now start. As part of our attempts to understand the unfolding crisis, we have asked three leading thinkers on the global economy – Jean-Pierre Lehmann, Kishore Mahbubani and Ethan Kapstein – to discuss the outcomes of the G-20 Summit. Based in Switzerland, the United States and Singapore, these respected economists bring their different regional perspectives to bear in a series of essays starting on page four. These essays were written in the first days after the summit and represent opinions, not answers. We put them forward in the hope that they help provoke thought and inform ongoing discussion.

As well as these essays, we have considered how our clients might be thinking about the decisions made in London on 2 April 2009. We have highlighted some of the key outcomes and the effects that these will have, both in the short term and the long term, on business around the world. This analysis starts on page 10.

The views of Jean-Pierre Lehmann, Kishore Mahbubani and Ethan Kapstein as reflected in this article are the views of the individual authors and do not necessarily reflect the views of Ernst & Young.

“This is the day that the world came together, to fight back against the global recession. Not with words but a plan for global recovery and for reform and with a clear timetable.”

Gordon Brown, Prime Minister, United Kingdom - Chair, London Summit

"This will be a turning point in our pursuit of global economic recovery. By any measure the London Summit is historic. It is historic because of the size and scope of the challenge that we face and because of the timeliness of our response."

Barack Obama, President, United States

G-20 London Summit overview

The G-20 - Group of Twenty - was founded in 1999 as an informal forum to promote discussion between industrial and emerging-market countries on key issues related to global economic stability. It was created as a response both to the financial crises of the late 1990s and to a growing recognition that key emerging-market countries were not adequately included in the core of global economic discussion and governance. It consists of the world's 19 largest economies - Argentina, Australia, Brazil, Canada, China, France, Germany, India, Indonesia, Italy, Japan, Mexico, Russia, Saudi Arabia, South Africa, South Korea, Turkey, United Kingdom, United States - plus the European Union. G-20 members represent 85% of the world's economic output.

It is normal practice for the G-20 finance ministers and central bank governors to meet once a year. To coordinate responses to the current global financial crisis, however, the leaders of the G-20 met in Washington D.C. on 15 November 2008, in London on 2 April 2009, and have pledged to meet once again in 2009.

At the London summit the gathered leaders agreed to measures that included:

Financial regulatory reform

- ▶ Extending financial regulation and oversight to all financial institutions, instruments and markets, including hedge funds and credit rating agencies
- ▶ Creating a new Financial Stability Board, with a strengthened mandate and expanded membership, to replace the Financial Stability Forum
- ▶ Endorsed new principles for sound compensation practices at major financial firms
- ▶ Calling on accounting standard setters to work with regulators to improve standards on valuation and provisioning and achieve a single set of global accounting standards
- ▶ Taking action against non-cooperative jurisdictions, including tax havens, that do not share information on request

IMF and other international financial institutions

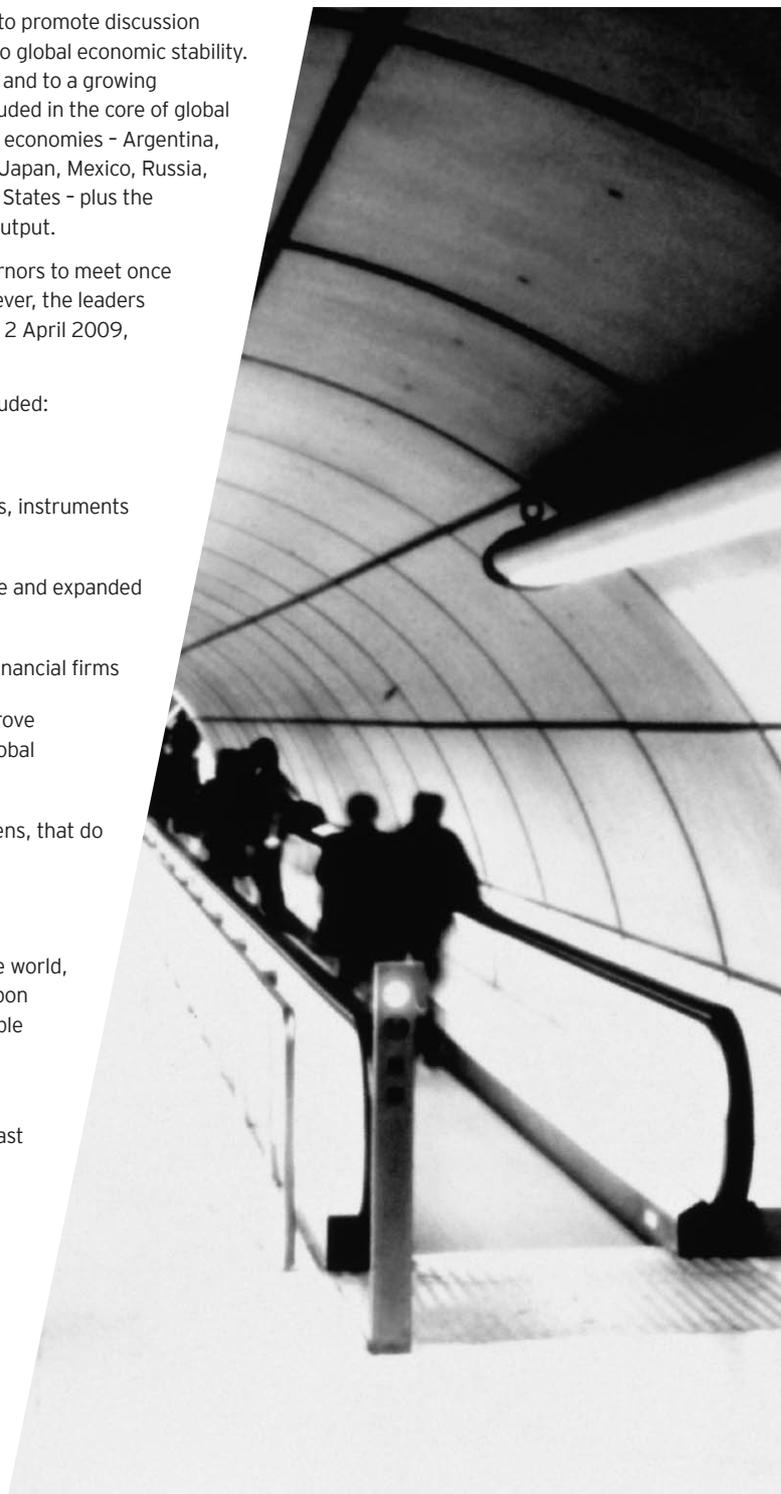
- ▶ Agreeing to make over US\$1 trillion available to economies across the world, representing an extraordinary commitment to growth, and building upon the first rounds of national fiscal stimulus packages. Resources available to the IMF will be trebled to US \$750 billion, including a new Special Drawing Rights allocation of US\$250 billion
- ▶ Supporting increased lending to the world's poorest countries of at least US\$100 billion by the multilateral development banks

Global trade and protectionism

- ▶ Committing to US\$250 billion of support for trade finance over the next two years
- ▶ Monitoring breaches of free trade rules

Fair and sustainable recovery

- ▶ Reaffirming commitments to both Millennium Development Goals and the Copenhagen UN Climate Change Conference



Caramels, bon-bons and chocolates

By Jean-Pierre Lehmann

Background

Jean-Pierre Lehmann, founding director of the Evian Group, has been Professor of International Political Economy at IMD International Institute for Management Development since January 1997. He has had both an academic and a business career which over the years has encompassed activities in virtually all East Asian and Western European countries, as well as North America. He acts in various leading capacities in several public policy forums and organizations. In 1995 Jean-Pierre Lehmann launched the Evian Group, which consists of high ranking officials, business executives, independent experts and opinion leaders from Europe, Asia and the Americas. The Evian Group's focus is on the international economic order in the global era, specifically the reciprocal impact and influence of international business and the WTO agenda.

When contemplating the G-20 London Summit, the best image is that of a large global religious ritual with all the high-priests assembled intoning the appropriate sutras that they imagine the faithful wish to hear. In reading the statement, however, one descends from high mass to low pop-music and especially the 1972 hit of the Italian singer Mina: Parole, Parole, Parole (Words, Words, Words), which she compares to "caramels, bon-bons and chocolates." Thus, throughout the text the "parole" duly appear: confidence, growth, jobs, trust, green, sustainable, inclusive, regulatory, and other "caramels, bon-bons and chocolates."

To give just one out of almost countless examples that could be cited: On the first page, paragraph four of the Statement, the leaders pledge "to do whatever is necessary to ... build a green recovery." And interspersed in much of the text one finds references to a "green economy." Nowhere in the text is there any indication of what that means let alone how it is to be achieved. In paragraph 27, all the way at the end, there is again reference to "building a resilient, sustainable, and green recovery" and to that end "we will make the transition towards clean, innovative, resource efficient, low carbon technologies and infrastructure." It is not as if we had not heard these (empty?) phrases before. An inkling of how this was going to be achieved would make a huge difference.

Jaw-jaw: better than war-war

It was, arguably, better that the Summit be held that it should not be held. Jaw-jaw, as Churchill said, is better than war-war. But this particular jaw-jaw does raise a lot of issues.

- 1) It is still not clear - nor have the meetings either in Washington or London clarified - what the legitimacy of the G-20 is, what are the criteria for composition of its membership and what is its mission.
- 2) The Summit does not seem in any way whatsoever to resolve the great challenge of our times, which is the systemic shift of global economic power from West to East. Both Washington and London were primarily Western affairs. The next meeting of Finance Ministers is scheduled to take place in Scotland. Why? Why not in Seoul or Jakarta? The G-20 will be seen by future historians as reflecting the end of the 20th (Atlantic) century - a sort of Western swansong - rather than ushering in the (Pacific) 21st century.
- 3) Indeed, historians will marvel that just as Europe is in decline - demographically and in other respects - there were no less than seven representatives from the EU, as opposed to one respectively from India, China, Indonesia, Brazil, US, etc.
- 4) The 20th versus 21st century paradigm was reflected in the membership, but also in the agenda. There were a number of issues raised that were quite blatantly included in order for Western politicians to pander to their domestic political public galleries - notably compensation and bank secrecy. These are not key issues for Brazil, China, India, Indonesia, Korea, etc, nor are they

"We have the enabling conditions to tackle the financial crisis. As long as we strengthen confidence and work together, we will tide over the difficulties and achieve our shared goals."

Hu Jintao, President, China

“The G-20 countries have decided on a commitment by heads of state and government to strengthen regulation and supervision of financial activities. That was a priority for Germany and France.”

Nicolas Sarkozy, the President of France

fundamental either to the causes or to the possible cures of the crisis. However one very critical issue that was flagrantly conspicuous by its absence in the Summit discussions is that of the future international currency. The Chinese suggestion that the dollar might conceivably be phased out was perhaps a bit half-baked - but a lot of what the G-20 discusses is half-baked - but that is not a reason for it to be ignored.

- 5) Providing all that money (or so it seems) to the IMF raises as many questions as it purports to provide solutions. The IMF has, very justifiably, a not entirely unblemished reputation. Even the IMF agrees that its medicine at the time of the East Asian

what does it mean?

- 8) No doubt the greatest failure and condemnation of the G-20 is in respect to trade and protectionism. First, though, while the allocation of \$250 billion to trade finance seems, on the face of it, highly commendable - and indeed there is a desperate need for trade finance - according to the FT (Alan Beattie & Jean Eaglesham, “Still no deadline for Doha Accord”, FT 2 April) the actual real new money going into trade finance amounts to about a tenth of the sum, ie \$25 billion, not \$250 billion. But much more dramatic - truly dramatic - is the vacuity and indeed mendacity of paragraphs 22 to 24 under the sub-heading:

“It has been five months since the Washington meeting—and yet we are still it seems entirely at the “we will” stage.”

financial crisis turned a crisis into a drama; and the method in which it was applied could be described as neo-imperialistically insensitive. (One should recollect the photograph of then IMF Head Michel Camdessus standing over then Indonesian President Suharto with his arms crossed as a bowed and cowed Suharto was signing what seemed - in many instances was - a rendition.) Does the IMF have the capabilities in terms of resources to allocate and manage this money effectively?

- 6) The G-20 Summit has in many respects a credibility problem between rhetoric and reality. How much of the money being talked about is real and new money as opposed to old and/or imaginary money? For example, in respect to the \$5 trillion (which sounds like a lot!), according to the FT the figure is the IMF estimate of the rise of the G-20 countries' increased government deficit and thus represents \$0 in terms of new commitments.
- 7) The G-20 Summit was hailed in some quarters as a success because a compromise had been found between the US insistent priority on stimulus and the Franco-German insistence on financial regulation. As suggested in [6] it is not clear how much of the stimulus is real. As to the financial regulation, a careful reading of the statement provides very little concrete sense of what such regulation might look like. In reading the text, it is striking to see the almost incalculable number of “we will’s” there are. It has been five months since the Washington meeting - which also produced a very “worthy” communiqué - and yet we are still it seems entirely at the “we will” stage. Thus, on the very critical issue of financial supervision and regulation, the text reads: “We will take action to build a stronger, more globally consistent, supervisory and regulatory framework for the future financial sector, which will support sustainable global growth and serve the needs of business and citizens.” Sounds great:

“Resisting protectionism and promoting global trade and investment.” The words are virtually the same as those contained in the similar rubric in the Washington declaration, with one important difference: in the Washington declaration there was a deadline set for the conclusion of Doha (end of the year 2008), whereas in this declaration it is left totally open-ended. The first bullet of paragraph 22 reads “we reaffirm the commitment made in Washington ... to refrain from raising new barriers to investment or trade in goods and services.” As the World Bank has “exposed”, 17 of the 20 did precisely that after Washington; they resorted to new protectionist measures. Without any recognition of past mis-deeds, how can it be expected that there should be any credibility at all in such a declaration of intentions. And in light of what has happened - ie nations cannot be trusted to honour their pledges - should there not be a system of sanctions put in place?

Grading the Summit

In assuming my professorial role, I would refuse to grade the G-20 statement. This is the second copy they have submitted. The first had to be sent back for revision. The second remains highly unsatisfactory, so it too must be rejected. I shall be very lenient and allow an extension to 30 November. By then I wish to see a statement of concrete achievements, a credible action plan, and not another declaration of motherhood intentions.

A turning point?

By Ethan B. Kapstein

Background

Ethan B. Kapstein holds the INSEAD Chair in Political Economy at INSEAD, and is Visiting Fellow at the Center for Global Development, Washington, DC. Previously he was Stassen Professor of International Peace at the University of Minnesota, Vice President of the Council on Foreign Relations, Principal Administrator at the Organization of Economic Cooperation and Development, and Executive Director of the Economics and National Security Program at Harvard University.

He is a former international banker and has served as an officer in the United States Navy. A specialist in international economic relations, he has published widely in professional and policy journals, and is a frequent contributor to the op-ed pages of the International Herald Tribune and Los Angeles Times. He is the author or editor of eight books, the most recent of which is *Economic Justice in an Unfair World*.

With stock markets rising around the world as soon as the London Summit ended, some American pundits were already declaring that the Summit heralds "the end of the Great Recession." President Barack Obama himself asserted that the Summit represented "a turning point in our pursuit of global economic recovery." Indeed, nearly the sole dissonant voice regarding the Summit that one could find anywhere was that of The New York Times editorial page, which flatly stated that the gathered leaders "fell short" of their responsibilities by not generating policies "to fix the global financial system and restore growth."

All these comments, whether positive or negative, represent a highly inflated view of economic summitry. Summits rarely represent the end - much less the beginning - of anything. Instead, they are part of an ongoing process of international negotiation and policy coordination that enables the global economy to function. So a more accurate question to ask of the Summit is this: did the world's leaders facilitate or impede the process of global economic cooperation during this period of acute stress?

The point of summitry

One might first ask, why are economic summits even necessary? After all, running the global economy is a highly technical business, requiring the elaboration and enforcement of a wide variety of regulations and soft laws across many different aspects of finance and trade. Normally, countries utilize functional specialists to negotiate over the arcane details of agreements within their cognate areas, so as to reconcile conflicting national practices that could impede international exchange. It would not be feasible or even desirable for a president or prime minister to become expert with respect to the details of the global systems that they try to govern.

What purpose, then, do summits fill? First, they enable leaders to meet and, in so doing, to gain trust in one another. This may sound vacuous, but in fact it is absolutely crucial to the smooth operation of any economic system; indeed, the current financial crisis again reminds us powerfully of what a central role trust plays in market processes. In a global economy, nations must trust one another to live up to their commitments to the finance and trade regimes. In the absence of such trust, systems cannot operate.

It is for this reason that newly elected President Franklin D. Roosevelt's absence from the 1933 London Economic Summit was such a grave mistake. Roosevelt was, at this time, relatively unknown in Europe, and those who did know him thought he possessed a "second-rate intellect." By failing to attend the Summit, the Europeans became convinced that he was a weak president, meaning that his public support was so low that he couldn't even risk leaving Washington for an international conference. As a consequence, there was little confidence that the United States would play a positive role in promoting economic recovery.

"It's the first meeting in which we weren't treated as if we didn't understand anything"

Luiz Inacio Lula da Silva, the President of Brazil

“We have agreed to set up a clear financial market architecture... We have taken an important step toward creating order in an area in the world where there was previously no order.”

Angela Merkel, Chancellor, Germany

A very different picture is offered by President Francois Mitterrand, whom many leaders distrusted before his attendance at summit meetings. There his outstanding intelligence impressed colleagues, giving him added clout in addressing the challenges the world faced during the 1980s. Indeed, one difference between the 1980s and today is the rapid convergence around policy solutions (e.g. the need for bank recapitalization) that the major industrial countries then adopted. Looking back, no single summit of that period represents either a beginning or an end of the crisis that erupted in 1982, but each contributed to the process of cleaning up bank balance sheets.

Second, and related, summits can provide market participants with confidence by re-iterating international commitments to longstanding institutional arrangements, such as those embodied by the International Monetary Fund and World Trade Organization. By reassuring market participants that the underlying structures of the global economy remain intact, agents become persuaded that the crisis is one that will be managed within the existing policy frameworks. In short, markets tend to like policy continuity and stability, and summits can confirm a commitment to the existing order.

for the International Monetary Fund, was written more in Washington than in Paris or Berlin. IMF funding therefore gets a 9/10.

That, in turn, provided market participants with confidence that the commitment to globalization remains strong. There can be no doubt that many emerging economies are facing severe hardship given the US-produced crisis, and that greatly increased funding for the IMF was sorely needed. Much of the expected shortfall will now be met through the trebling of resources that will be made available for IMF programs. The commitment to completing the Doha Round of the World Trade Organization was also welcome, if much less credible given the protectionist actions now being adopted almost everywhere.

More questionable, however, concerns the priorities that follow after the IMF (and trade credit) package. The Summit was relatively silent about the problems facing the banking system, which remains at the heart of the world's economic headaches. Yesterday markets seemed willing to overlook that shortfall, but for how long will that remain the case? Providing reassurance that viable policies are being formulated to meet international financial challenges remains

“summits are useful to the extent that they promote trust among leaders, generate confidence among market participants, and establish policy priorities for action.”

Third, economic summits can provide guidance with respect to policy priorities. During the economic crises that followed the 1973-74 oil shocks, for example, leaders determined that their priority should be to stimulate their economies, a position that even the Germans would eventually accept (of course, it should be recalled that these policies are often credited with generating “stagflation”!)!

In summary, economic summits are useful to the extent that they promote trust among leaders, generate confidence among market participants, and establish policy priorities for action. These are the broad measures that can promote the technical processes needed to confront economic challenges in a collective and cooperative matter. Alternatively, a failed summit would be one in which leaders demonstrated their incapacity to work together, expressed doubts about their commitment to the global economy, and proved incapable of setting priorities.

Grading the Summit

Clearly, the Summit provided President Barack Obama with his first opportunity to shine on the global stage. He took full advantage and claimed center stage in his uniquely laid-back manner.

The “headline” from the Summit, which focused on new money

the biggest missing piece from the London Summit.

Relatedly, in my view, the discussion of regulatory reform at the Summit was quite vague, and sounded much like previous statements that we've all heard during previous crises (e.g. about the need to create “early warning systems,” a call which goes back at least to 1982 if not before). Personally, I do not believe that regulatory reform should be a major priority at the present time, so perhaps that's all to the good. But those who are looking for stronger direction in this area are likely to be disappointed, and would probably give regulatory reform at the Summit a grade of 3/10.

The Summit also gave markets little guidance about additional fiscal stimulus packages at the national level in such large economies as those of the European Union, China, or Japan. In fact, the European Central Bank's smallish interest rate cut indicates that at least some European officials now believe that it is time to draw the line against further spending. Again, for those who were looking for a stronger national commitment to spend one's way out of the crisis, the grade here can only be 1/10.

An Asian perspective

By Kishore Mahbubani

Background

Former Singaporean Ambassador to the United Nations Kishore Mahbubani is the Dean and Professor in the Practice of Public Policy, Lee Kuan Yew School of Public Policy, National University of Singapore. He has spoken and published globally. His articles have appeared in a wide range of journals and newspapers, including *Foreign Affairs*, *Foreign Policy*, the *Washington Quarterly*, *Survival*, *American Interest*, the *National Interest*, *Time*, *Newsweek* and *The New York Times*. He has also been profiled in *The Economist* and *Time*. He is the author of "Can Asians Think?" and of "Beyond The Age Of Innocence: Rebuilding Trust between America and the World" (published in New York). His new book entitled "The New Asian Hemisphere: the irresistible shift of global power to the East" was published in February 2008.

The G-20 is not an event. It is a process. Some meetings will succeed. Some will fail. But the process will continue as it is well designed to manage the biggest shift of power in millennia: the Rise of Asia. And the rising weight of Asia was reflected in some key points of the London communiqué.

The biggest achievement of the London meeting was that it did not fail. This may be one reason why markets reacted favourably to its conclusion. In the build up to it, there were warnings that the meeting would break down. Sarkozy threatened to walk out. The western media played up the tension between the American emphasis on fiscal stimulus and the European emphasis on regulation. In the end, the meeting was saved by the oldest trick in diplomacy: creative fudging. This enabled all to claim victory.

The London communiqué, as per usual British standards, was beautifully crafted. It even had some memorable phrases: "A global crisis requires a global solution" and "We will not repeat the historic mistakes of protectionism of previous eras." The communiqué also had some impressive numbers. The G-20 promised to inject US\$1.1 trillion to stimulate the global economy. But several analysts were quick to point there was little new money put on the table. Obama may have been premature in suggesting that the Summit could mark a "turning point." It is more than likely that the global economy will continue to have a rough time in the coming months and years.

The Asians did not participate in the American-European debate about stimulus versus regulation. They welcomed both. However, when the West asked for greater funds for IMF, the Asians demanded and received an assurance of greater say in the management of both the IMF and World Bank. One of the most anachronistic rules of our times is the stipulation (reiterated as recently as 2007) that the head of the IMF had to be European and the head of the World Bank an American. The London communiqué said, "we agree that the heads and senior leadership of the international financial institutions should be appointed through an open, transparent, and merit-based selection process." This is a significant concession by the US and Europe. However, real change will come only when Europe agrees to reduce its voting share in the IMF. It still has 32% compared to China's less than 4%.

G-20 versus G-2

This less-than-4% figure does not represent well China's growing economic weight in the world. Soon it will go from being the third largest economy to the second largest economy in the world. Hence, many say that the world should pay greater attention to G-2 (US and China) rather than the G-20 process. And, in the build-up to the G-20, China sent some powerful signals that it was not entirely happy with American management of the global economic order. Sarkozy had to threaten a walkout to gain attention. China did it more subtly by getting its Central Bank governor, Zhou Xiaochuan, to deliver a thoughtful speech on the need to look for alternatives to the US Dollars

"Twenty or 25 years ago it would be impossible to imagine a situation when so different nations, with so different economies, various mentalities and historical traditions could sit down at the same table and be able to agree on how to act in such a complicated situation, and to do it fairly fast!"

Dmitry Medvedev, President, Russia

"We welcome the tremendous degree of cooperation between public and private sector institutions that allows us to come together to launch the Global Trade Liquidity Program for developing countries. I welcome G-20 support for this timely and targeted solution that will provide trade finance to support businesses across developing markets."

Robert B. Zoellick, President, World Bank Group

as an international reserve currency. He got a lot of attention.

There have been many analyses of Zhou's speech, mostly by economists. Many have pointed out the strengths and weaknesses of his economic arguments. Few of these economists noticed that there was another dimension at play in Zhou's remarks: the geo-political dimension. China had managed its rise well by creating a mutual interdependence between the world's greatest power (the US) and the world's greatest emerging power (China). China depended on the US for markets for its products; the US depended on China to buy US Treasury Bills. This is why at the height of the crisis both Dave McCormick of the Bush administration and Hillary Clinton of the Obama administration had gone to Beijing to seek and obtain an assurance that China would continue to buy US T-bills.

This mutual interdependence was severely threatened by a pre-emptive American move. Bernanke announced on 18 March that the Fed would purchase up to \$1.2 trillion of US Treasury bills and government bonds. Essentially this meant that the US would print money to purchase US T-bills. This would inevitably lead to inflation and devaluation of the stock of the US T-bills that China has accumulated. Equally importantly, the US dependence on China would decrease. This Chinese worry may explain the inclusion of this sentence in the London communiqué, "We will conduct all

From all accounts, Obama was the star of the G-20 meeting. His personality works well in multilateral settings. It helped that his wife Michelle, also emerged as a media star. This promising start augurs well for the future of multilateralism in the Obama administration.

A glimpse of the future

A stronger American commitment to strengthening multilateral institutions and processes would help Asia enormously. As the biggest beneficiaries of the global liberal trading order created by the US and Europe after World War II, the emerging Asian economies, especially China and India, have the most to lose from any retreat from this order. Both the earlier November 2008, Washington DC and the latest London communiqués were replete with references on the need to preserve and strengthen multilateral institutions. If this can be balanced with greater Asian representation on the decision-making processes of these institutions, the G-20 process will inevitably help to engineer a smooth transition to a new historical era. And this long-term contribution may be as important as any short-term gains that the G-20 meetings may deliver. This is also why the Asian countries will cheer on the G-20 process in the hope that it will eventually bury the G-8 process. The G-8 meetings provide a postcard from the past. The G-20 meetings provide a glimpse into the future.

"A stable and cooperative US-China relationship is an essential prerequisite for the world returning to the era of stable long-term growth."

our economic policies cooperatively and responsibly with regard to the impact on other countries and will refrain from competitive devaluation of our currencies and promote a stable and well-functioning international monetary system." The subsequent sentence called for "candid, even-handed, and independent IMF surveillance of our economies and financial sectors, of the impact of our policies on others." Taken together, these sentences indicate that other countries would like the US to pay greater attention to the impact of its unilateralist policies.

This background also explains why one of the most important bilateral meetings in London was the Obama-Hu Jintao meetings. From all accounts, it seems to have gone off well. A stable and cooperative US-China relationship is an essential prerequisite for the world returning to the era of stable long-term growth. If Obama and Hu can work out a sound long-term understanding - with the help of the G-20 framework - we can afford to become optimistic again.

Unlike the Bush Administration, which began with a strong aversion to multilateral institutions and processes (which it later had to backtrack from), the Obama administration has begun with a strong preference to work with multilateral institutions and processes.

Grading the Summit

1. Regulatory reform - Agreeing the basis of a new regulatory architecture: 5
2. Fiscal stimulus - Agreeing a cross border approach to fiscal stimulus: 3
3. IMF funding - Providing sufficient funding to the IMF: 7

What the Summit means for business

The G-20 summit may have been a political event, but it also signalled the beginning of a new era for business. CEOs will be operating in a very different - and, for many, less favorable - business environment. We see five key implications that businesses need to be thinking about in light of the outcomes of this meeting:

1) The new economic order

A key theme of this summit was the shift of power from west to east and north to south: the existence of the G-20 in itself (in contrast to the historic G-7 and G-8) marked this, as did President Obama's comments on America's revised role on the global stage in his post-summit conference. The pivotal role that emerging economies have played (and will play in the future) was acknowledged, and 'rewarded' by proposed changes to the structure of the IMF - although many would argue there is still some way to go to make these institutions and processes truly representative of the new economic order.

Businesses in the 'old world' need to understand what this continuing evolution of the global business landscape means: they will need to adapt, whether the G-20 commitments to fight protectionism are enforced or the growing trend towards stealthily introduced trade

currently unregulated in some jurisdictions - will move from 'shadow banking' into the more regulated sphere. Credit rating agencies also will now be regulated. We are also likely to see a reduction in complex and opaque products, and higher standards on anything that may mitigate potential risk - for example, capital ratios in banking. While the G-20 has been careful to word its restrictions on capital and leverage as actions to be followed through "when recovery is assured" (with the aim of minimising any barriers to growth in the short term), it seems likely that the spirit of these recommendations will be felt immediately.

The financial sector will not be alone in feeling the squeeze from this regulation; these restrictions and increased supervision will impact all sectors. Changes to compensation packages, aligning them to longer-term goals and prudence in risk-taking, for instance, will be most keenly felt in the financial world, but the principles adopted may also begin to extend to businesses across the board. The G-20 agreements also reiterated the goal of a "single set of high-quality global accounting standards", and included a call for the accounting standard setters to work with regulators and supervisors to improve standards on valuation and provisioning. While the exact implications of this statement may not be clear for some time, it is clearly a response to the current debate

"The G-20 signalled a move towards greater responsibility, long-term oversight, and improved risk management"

restrictions continues. Corporations will need to invest more heavily in emerging economies, if they are not already doing so, and understand where the threats to their business or consumer base may come from. As with the international financial institutions, they will need to consider whether their leadership and organization is still appropriate and representative. They will also need to assess the different risks and sensitivities, including cultural differences, that come from operating more globally.

Businesses in the emerging economies will also need to adapt. To take advantage of the global marketplace, some companies will need to adopt new working practices: along with greater visibility will come a requirement for higher standards and greater accountability. Greater geographic reach will drive changes for all companies - in developed and emerging companies: they will need to find access to funding on a more global basis, to build global supply chains, and to understand a broader consumer base.

2) Fundamental changes to the financial and regulatory landscape

The biggest changes to the financial sector will be in its regulation and oversight. The newly reconstituted Financial Stability Board strives to identify and address risk across jurisdictions, and takes "all systemically important financial institutions, instruments and markets" under its watch. As 'systemic importance' will be a function of what institutions do, rather than their legal form, institutions such as hedge funds -

over mark-to-market (although, crucially, not an outright rebuttal of the principles behind it), and we anticipate this may bring further changes to how businesses across the world report their financials in the future.

Finally, the Summit and its outcomes continue to illustrate the far greater government involvement in the financial and regulatory landscape that we began to see in the national actions leading up to the G-20. Politicians and civil servants will hold significantly more power than before and, given the vast sums of money invested, will be intent on wielding this power to achieve the best outcome for their constituents across the globe. Business also needs to be cognizant of the greater risk of protectionism that comes with increased government involvement: barriers may be put up to protect government-owned businesses, or to discourage foreign government-owned businesses from taking stakes in strategic industries.

3) A greater focus on responsibility and risk management

The G-20 signalled a move towards greater responsibility, long-term oversight and improved risk management: principles and ethics will become a more important component of business strategy, as companies consider the impact their activities and decisions have on the world around them. A move towards greater long-term planning around risk management is one part of this. Risk management processes will have to give greater consideration to full economic cycles over longer periods, rather than just the immediate economic circumstances. Practices and regulatory environments that allowed too

"The important thing is that there is, as in other areas of the G-20 work yesterday, convergence, unanimity on the view that in order to respond to this crisis, trade must remain open."

Pascal Lamy, Director General, World Trade Organisation

“The global crisis is hitting emerging market and poor countries hard. The G20 leaders have today sent a powerful signal that the international community is committed to support these countries”

Dominique Strauss-Kahn, IMF Managing Director

much risk to go unchecked (and, indeed, encouraged it through compensation) will have to be curtailed. And implementing risk management and governance frameworks that meet the needs of regulators, investors and governments will be an important factor for almost all businesses and sectors. While the exact approach will clearly vary depending on a company's size and location we will likely see a more sophisticated approach to risk management coming into the mainstream. The winners will be those who manage to implement this risk management approach without stifling all innovation, and without allowing it to become too costly.

A longer-term view on businesses' and humanity's impact on the planet also emerged - responsibility in its broadest sense. Not only was there an affirmation of the importance of the Copenhagen climate change conference in December 2009, but there was a commitment to use fiscal stimulus programs (where they occur) to build a green and sustainable recovery - which may herald a new wave of investment in low carbon technology and infrastructure, which some companies will be well positioned to take advantage of.

4) Changes to the tax environment

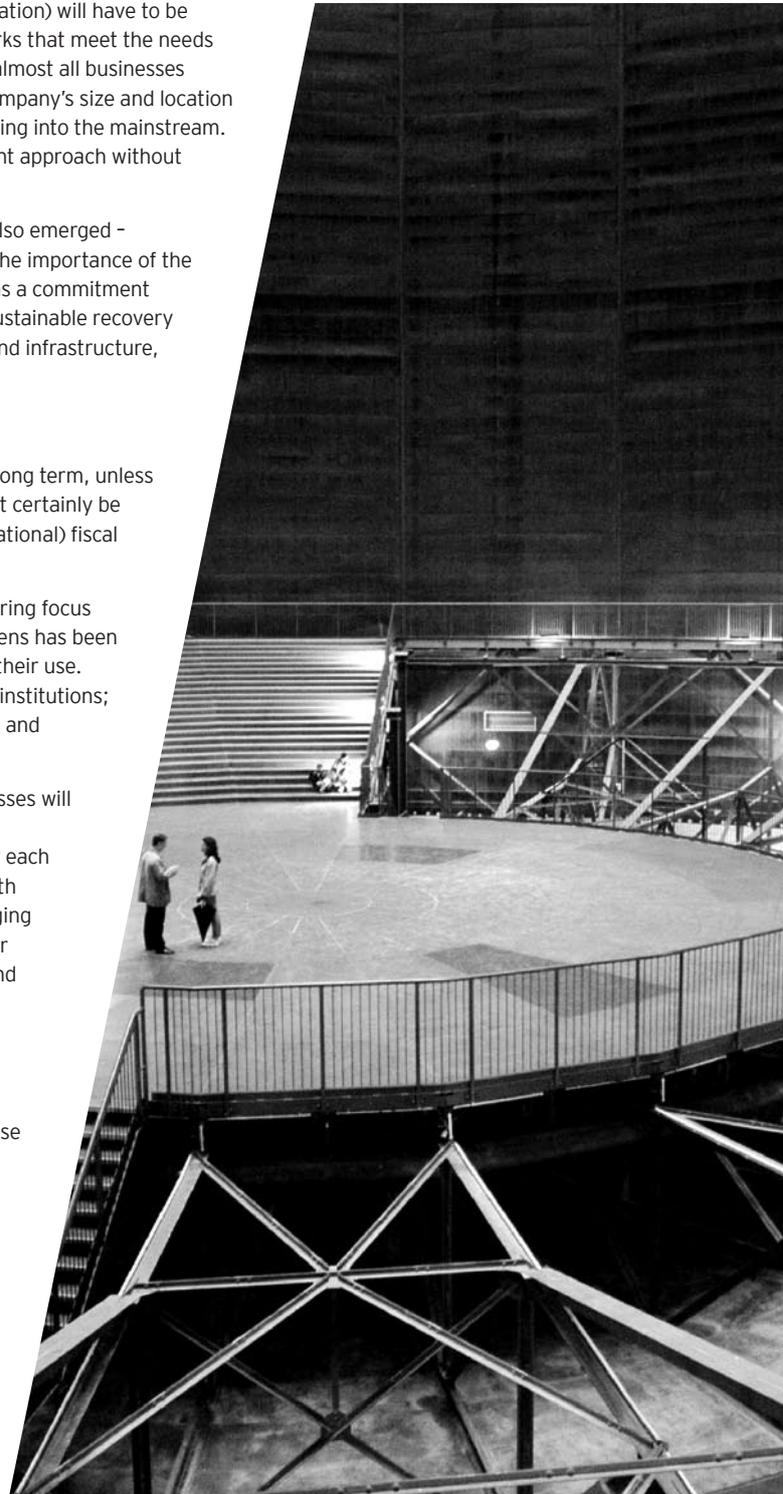
The decisions made by the G-20 participants will not come cheap. In the long term, unless governments are able to control or limit public expenditure, we will almost certainly be moving into a sustained period of higher taxation to foot the bill of the (national) fiscal and (global) monetary stimulus packages.

The issue of increased transparency and raising revenues will inevitably bring focus on a number of areas. For example, the approach to the future of tax havens has been the subject of vigorous debate and many governments may wish to limit their use. We will see increased disclosure requirements on taxpayers and financial institutions; it is also likely that tax treaties will have greater emphasis on cooperation and openness.

This is not just about tax havens: the broader tax environment for businesses will become increasingly challenging as tax authorities seek to bolster falling revenues. For instance, transfer pricing policies are already a key area for each government to focus on and are giving rise to a greater number of in depth enquiries. While businesses will continue to seek effective ways of managing their tax liabilities there is no question that they are already under greater scrutiny. This will require all businesses to have effective strategies around managing their tax risks going forward.

5) A new type of opportunity

Not all the changes will create a more difficult business environment. In a period of such significant flux, the businesses that flourish will be those that are continuously scanning the horizon to identify the opportunities. For instance substantial portions of the funds committed by the G-20 - and by individual nations - will go towards large-scale infrastructure improvements and green technology. Businesses that are able to access these kind of stimulus program credits or are in the 'right' sector could benefit substantially from the economic downturn. Equally, the quickly changing competitive landscape (with current players failing, and new entrants - particularly governments - emerging in many sectors) provides opportunities for astute businesses.



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