

BRUSSELS FORUM  
PAPER SERIES

**SAVING MULTILATERALISM**  
*RENOVATING THE HOUSE OF GLOBAL ECONOMIC GOVERNANCE  
FOR THE 21<sup>ST</sup> CENTURY*

**JENNIFER HILLMAN**  
THE GERMAN MARSHALL FUND OF THE UNITED STATES



© 2010 The German Marshall Fund of the United States. All rights reserved.

No part of this publication may be reproduced or transmitted in any form or by any means without permission in writing from the German Marshall Fund of the United States (GMF). Please direct inquiries to:

The German Marshall Fund of the United States  
1744 R Street, NW  
Washington, DC 20009  
T 1 202 683 2650  
F 1 202 265 1662  
E [info@gmfus.org](mailto:info@gmfus.org)

This publication can be downloaded for free at <http://www.gmfus.org/publications/index.cfm>. Limited print copies are also available. To request a copy, send an e-mail to [info@gmfus.org](mailto:info@gmfus.org).

#### **GMF Paper Series**

The GMF Paper Series presents research on a variety of transatlantic topics by staff, fellows, and partners of the German Marshall Fund of the United States. The views expressed here are those of the author and do not necessarily represent the view of GMF. Comments from readers are welcome; reply to the mailing address above or by e-mail to [info@gmfus.org](mailto:info@gmfus.org).

#### **About GMF**

The German Marshall Fund of the United States (GMF) is a non-partisan American public policy and grant-making institution dedicated to promoting greater cooperation and understanding between North America and Europe.

GMF does this by supporting individuals and institutions working on transatlantic issues, by convening leaders to discuss the most pressing transatlantic themes, and by examining ways in which transatlantic cooperation can address a variety of global policy challenges.

Founded in 1972 through a gift from Germany as a permanent memorial to Marshall Plan assistance, GMF maintains a strong presence on both sides of the Atlantic. In addition to its headquarters in Washington, DC, GMF has seven offices in Europe: Berlin, Bratislava, Paris, Brussels, Belgrade, Ankara, and Bucharest.

#### **About Brussels Forum**

Brussels Forum is an annual high-level meeting of the most influential American and European political, corporate, and intellectual leaders to address pressing challenges currently facing both sides of the Atlantic. Participants include heads of state, senior officials from the European Union institutions and the member states, U.S. Cabinet officials, Congressional representatives, Parliamentarians, academics, and media. For more information, please visit [www.brusselsforum.org](http://www.brusselsforum.org).

# SAVING MULTILATERALISM

*Renovating the house of global economic governance for the 21st century*

BRUSSELS FORUM PAPER SERIES

MARCH 2010

Jennifer Hillman\*

The German Marshall Fund of the United States

|   |    |
|---|----|
| Introduction: Coping with Complexity . . . . .                                    | 3  |
| Solid Foundations: The Architecture of Global Economic Governance . . . . .       | 6  |
| The Great Recession and the Steering Committee of the World Economy . . . . .     | 10 |
| The IMF, World Bank, and WTO: From Crisis to Reform. . . . .                      | 15 |
| Guardian of Global Finance: The International Monetary Fund . . . . .             | 17 |
| From Reconstruction to Development: The World Bank . . . . .                      | 20 |
| Negotiating the Rules: The World Trade Organization . . . . .                     | 24 |
| Renovating the House of Global Economic Governance for the 21st Century . . . . . | 27 |
| The Harbinger of Global Governance: Political Leadership and the G20 . . . . .    | 28 |
| Reaffirming Multilateralism in a World of Regionalism . . . . .                   | 30 |
| Transatlantic Multilateralism for the 21st Century . . . . .                      | 33 |
| Conclusion . . . . .  | 37 |
| Bibliography . . . . .  | 38 |

\*Jennifer Hillman is a senior transatlantic fellow at the German Marshall Fund of the United States and a current member of the World Trade Organization's Appellate Body. Previously, she served as commissioner at the U.S. International Trade Commission and general counsel and chief textiles negotiator at the Office of the U.S. Trade Representative. The author would like to thank Joe Guinan, Roman Balin, Dan Price, Peter Sparding, Debra Steger, and Kati Suominen for their help with this paper.

# 1 INTRODUCTION: COPING WITH COMPLEXITY

Last December, the eyes of all those with a stake in international affairs turned to Europe. First they looked to Geneva, for signs that the long-running Doha Round of multilateral trade negotiations at the World Trade Organization (WTO) would get back on track after years of stalemate. Then observers turned to Copenhagen, hoping to see a binding and comprehensive agreement reflecting a commitment on the part of the world's governments to address the pressing global challenge of climate change. They were to be sorely disappointed. Inscribed on the faces of those struggling to reach agreements was a deep frustration with multilateral processes that were proving incapable of delivery. Instead of agreement, the images playing out on television screens and in newspapers around the world were of fractiousness and division, due in part to the large number of participants and contentiousness of the issues faced; of anger, on the part of all those who felt marginalized by the process; and of concern, from those looking for signs that the world still has the capacity to reach accords when it really matters.

The failure of these meetings to produce formal agreements—or even specific paths to reaching agreements in the future—despite the high stakes and the political capital that had been invested in advance left many questioning the ability of the world's leaders to meet global challenges, shedding a spotlight on the institutions and fora that were established for the purpose of achieving multilateral solutions to the most pressing collective problems of the 21st century.

Why did these meetings fail? Many had assumed that the most significant economic crisis since the Great Depression and the overwhelming scientific and circumstantial evidence of damaging changes to our climate would compel world leaders to set aside their differences and reach meaningful agreements. But it did not happen. It is not that the problems are not big enough or urgent enough. The

failure to reach agreements can best be seen as part of a long-term trend toward increased complexity in the world that makes it nearly impossible to reach traditional multilateral binding accords, combined with a waning of faith on the part of many countries in multilateralism and multilateral institutions.

This increased complexity stems from a number of seismic shifts in international relations—and especially in international *economic* relations—some of which have been unfolding over the course of decades while others are of more recent origin. Government policies and international arrangements for collective decision-making have not kept pace with changes in the world, especially the high degree of international economic integration and interdependence. With decolonization came increases in the number of countries who are players on the world stage as well as a rebalancing of global economic power that has continued with the rise of the BRICs (Brazil, Russia, India, and China) and the other emerging market economies. The collapse of the Soviet bloc, accompanied by market reforms in China and India in the 1980s and 1990s accelerated the rapid integration of the global economy. Where previously only about half the world's population—the Organisation for Economic Co-operation and Development (OECD) countries, plus parts of Latin America and Asia—were engaged in global economic activity, suddenly people everywhere were brought together in a single world economy based on capitalism and markets.

At the macro-level, this led to shifting trade flows and patterns of foreign direct investment, a rise in the number and size of multinational companies and financial institutions, and surging global demand. It also meant a corresponding increase in the speed with which goods, money, and technology traverse the globe. At the micro-level, the “great doubling” of the

*The long-term trend toward increasing complexity combined with a waning faith in multilateralism and multilateral institutions makes it nearly impossible to reach traditional binding multilateral accords.*

*The inability to create new institutions or reach agreements means greater reliance on—and greater need for renovation of—the existing international economic institutions, the IMF, the World Bank, and the WTO.*

global workforce has had a direct effect on wages, income levels, and employment in the advanced industrial countries, in some instances prompting fears of economic insecurity and a public backlash against “globalization.”<sup>1</sup>

Taken together, all these factors have stretched the capacity of the current institutions of multilateral governance to a breaking point, leading to fragmentation and the emergence of deep divisions among groups of countries at different stages of economic development. Throw in the increases in the complexity of the issues themselves and the degree to which these issues overlap and affect one another and the problems of the 21st century begin to look too complex to handle.

This paper argues that learning to operate in this vastly more complex world will require more multilateralism, not less. It means greater reliance than ever on those economic institutions and fora that have already learned to function in a global fashion—particularly the World Bank, the International Monetary Fund (IMF), and the WTO. It contends that creating new international institutions or binding accords is nearly impossible in today’s world, and examines where the existing institutions stand today and the changes that will be necessary if they are to form the core of an effective global economic architecture for the 21st century.

Secondly, the paper explores the problems created by the lack of faith in multilateralism, particularly on the part of many developing and emerging market countries, who either don’t want to rely on the multilateral institutions designed in a bygone era when the transatlantic powers dominated the world or who find that their economic needs can be more easily addressed through bilateral or regional agreements rather than working through the often

more cumbersome processes at the multilateral level. Despite a new multilateralist president in the United States, the momentum in the world of global governance today is in the wrong direction, to be found in the hundreds of regional, sub-regional, and bilateral agreements that have come into force in the last several decades. With each such agreement comes a lessening of the energy, time, and resources left for multilateralism and multilateral institutions—along with the hard fact that the toughest global problems thus remain on the table, unsolved and insoluble through such regional arrangements.

Third, the paper contends that, in the absence of any prospect of building a new global economic architecture, the existing institutions of multilateral economic governance must be “renovated.” Their governance structures need to be changed to reflect the dramatic shifts in the distribution of economic weight among countries, their mandates revised in order to ensure that they cover a wider range of issues but with better coherence among them, and they must be adapted in the face of proliferating regionalism, with a shift toward accommodating and incorporating regional accords within multilateral frameworks.

This paper also contends that while these changes are both daunting and essential if the institutions are to have the efficiency, effectiveness, and legitimacy they require, they are in fact well within the grasp of the current world system. We are not, in other words, in “a 1944 moment”—the constitution-making epoch when the United Nations, along with the World Bank, the IMF, and the predecessors to the WTO were created largely out of whole cloth. Nor do we need to be in such a moment in order to achieve a global economic architecture capable of meeting the needs of the 21st century. The current crisis, the coming together of world leaders through the elevation of the G20, and a common understanding of the

<sup>1</sup> Richard B. Freeman, *America Works: Critical Thoughts on the Exceptional U.S. Labor Market* (Russell Sage Foundation, 2007).

failings of the current international economic institutions ought to be enough to compel these much-needed renovations of the system.

Finally, although leadership will be needed from countries all around the world, the paper concludes by suggesting the role that Europe and the United States must play if they are to

help save what together they started 65 years ago—the institutions of a multilateral economic order created to bring about global peace and prosperity for all, with a commitment to think and act globally when addressing the most pressing economic problems of the day.

## 2 SOLID FOUNDATIONS: THE ARCHITECTURE OF GLOBAL ECONOMIC GOVERNANCE

*The UN bore responsibility for issues of diplomacy, security, and war; the World Bank for international development and the reduction of poverty; the International Monetary Fund for financial stability and economic cooperation; and the GATT, precursor to the World Trade Organization, for trade liberalization and institutional stability in the world trading system.*

In 1944, in the woods of New Hampshire, with the end of World War II already in sight, an extraordinary set of gatherings occurred, bringing together an array of government officials whose vision for a better future was shaped by the hard lessons of the 1930s. Rejecting the catastrophic “beggar-thy-neighbor” policies of the major economic powers that had hastened the slide into worldwide depression and war, these public servants dedicated themselves instead to the creation of a rules-based international economic order that would serve as the basis for peace and prosperity. Over the course of the Bretton Woods Conference, the subsequent Dumbarton Oaks and San Francisco meetings, and the months that followed, they conceived of and created the charters for four major international institutions—the United Nations (UN), the International Bank for Reconstruction and Development (World Bank), the International Monetary Fund, and the International Trade Organization (ITO).<sup>2</sup>

At their inception, each of the major international institutions played specified roles. The UN bore responsibility for issues of diplomacy, security, and war; the World Bank for international development and the reduction of poverty; the International Monetary Fund for financial stability and economic cooperation; and the GATT, precursor to the World Trade Organization, for trade liberalization and institutional stability in the world trading system.

These institutions, while far from perfect, have done much to accomplish their most fundamental goals. In light of the tremendous pressure from around the world to protect domestic markets

and jobs, the GATT/WTO and its rules and disciplines have kept an outbreak of Depression-era protectionism at bay for half a century, and eight rounds of multilateral trade negotiations have resulted in widespread liberalization of trade—at least in industrial products among industrial countries. The UN, while not achieving the ultimate goal of bringing an end to all wars, has done much to contain crises, settle regional conflicts, man peacekeeping missions, eradicate diseases, and work out agreements on everything from human rights conventions to the use of the seabed and of outer space. Similarly, the World Bank, while not eliminating poverty, has seen the portion of the world’s population living in poverty decline from 40 percent 20 years ago to 21 percent today, along with providing loans and development assistance in more than 126 countries and participating in initiatives on everything from combating HIV/AIDS to biodiversity to education and debt relief for the poorest countries. The Bank is rightfully commended for its ability to raise and channel resources for development, for its highly-trained staff, and for its depth of knowledge about development strategies and approaches across country boundaries.<sup>3</sup> The IMF, while it has evolved considerably from its initial days of monitoring adherence to the par value system of fixed exchange rates, has made important changes to its key instruments—surveillance, lending, and technical assistance—allowing it to contain a number of financial crises, continue concessional lending where necessary, and join the fight against extreme poverty.<sup>4</sup>

<sup>2</sup>The UN, IBRD (World Bank) and IMF all came into being with little delay. However, attempts to launch the ITO with a broad mandate had to be abandoned in 1951 when the Truman Administration announced that it would not seek ratification of the Havana Charter due to lack of support in the U.S. Congress. Instead, in 1947 a smaller group of countries negotiated the General Agreement on Tariffs and Trade (GATT), which was transformed in 1995 into the World Trade Organization (WTO).

<sup>3</sup>“Repowering the World Bank for the 21st Century.” *Report of the High-Level Commission on Modernization of World Bank Group Governance* (the “Zedillo Commission Report”), Oct. 2009, p. 9.

<sup>4</sup>Rodrigo de Rato, former managing director of the IMF took the view before the 2008-2009 financial crisis that fundamental reform to the IMF was not needed, arguing that the IMF had evolved over its 60 years through amendments to its key instruments while remaining true to its purposes of fostering international economic cooperation, promoting rising prosperity and safeguarding global financial stability. Rodrigo de Rato, “Is the IMF’s Mandate Still Relevant?” *Global Agenda*, Jan. 2005.

For their part, the United States and the member states of the European Union have been among the most active and engaged participants in these institutions. This is unsurprising, given the role the transatlantic partners played in creating these institutions and the interests they were originally intended to serve. At bottom, the postwar global economic architecture was established as a means to tie the West together

in the emerging Cold War context through the liberalization of international trade and capital flows. First through the institutions of the Bretton Woods system, and then through the Marshall Plan, the United States was able to rebuild the shattered production capacity and financial markets of Western Europe. For the United States, the overriding purpose was clear: the political-strategic need to build up a bulwark against

| Table 1. The architecture of global economic governance  |   |   |
|--|---|---|
| International Monetary Fund (IMF)  | World Bank  | World Trade Organization (WTO)  |
| <b>Began with:</b> 44 members  | <b>Began with:</b> 44 members   | <b>Began with:</b> 23 GATT parties  |
| <b>Now:</b> 186 Members  | <b>Now:</b> 186 Members   | <b>Now:</b> 153 Members   |
| <b>Mandate:</b> <ul style="list-style-type: none"> <li>• Promotes international monetary cooperation</li> <li>• Macroeconomic surveillance</li> <li>• Promotes exchange stability</li> <li>• Develops multilateral system of payments</li> <li>• Makes resources available to member's experiencing balance of payments difficulties.</li> </ul> | <b>Mandate:</b> <ul style="list-style-type: none"> <li>• Evolved from facilitator of post-war reconstruction and development to mandate of worldwide poverty alleviation</li> <li>• Promotes long-term economic development by providing technical and financial support</li> <li>• Funds loans through member country contributions and bond issuance</li> </ul> | <b>Mandate:</b> <ul style="list-style-type: none"> <li>• Forum for trade negotiations</li> <li>• Handles trade disputes through dispute settlement process</li> <li>• Monitors and implements trade agreements</li> <li>• Technical assistance and training for developing countries</li> <li>• Cooperation with other international organizations</li> </ul> |
| <b>Revenue:</b> \$325 billion in quotas contributed by members (as of 3/09)  | <b>Revenue:</b> In 2009, IBRD raised \$44.3 billion. In FY 09–11, commitments of \$41.7 billion made available to IDA   | <b>Revenue:</b> Administrative budget of \$173 million, paid by contributions from members based on a share of world trade  |
| <b>Loans or grants:</b> \$175.5 billion in loans committed, of which \$124.5 billion not drawn (as of 9/09)  | <b>Loans or grants:</b> \$58.8 billion in total commitments (loans, credits, guarantees, and grants) in 2009  | <b>Loans or grants:</b> \$28 million of training and technical assistance provided; support for Aid for Trade initiatives   |

Source: IMF, World Bank, WTO websites



*The legacy of this history is that the United States and Europe enjoy outsized control at the Bretton Woods institutions.*

Communism. But it also served U.S. economic self-interest: a significant portion of Marshall Plan aid effectively went to boost European demand for goods from the United States, helping stave off domestic fears of a postwar slump or renewal of the Great Depression. Over the medium term, the Bretton Woods system helped create foreign markets for the United States by conjuring up a middle class in U.S. economic partners around the world, something from which the Europeans—once they were back on their feet following the Marshall Plan and the reconstruction program of the Organization for European Economic Cooperation—have also been able to benefit. Today, by way of illustration, nearly one-third of U.S. and EU exports are to developing countries where the World Bank has lending programs.

By together establishing the rules and standards of conduct by which the global economy is governed, the United States and European Union became the stewards of the international economic order, running the system for much of the postwar era. In return, the three pillars of the global economic architecture they established—covering the financial side of economies (IMF), trade in goods and the real side of economies (GATT/ WTO), and international development and poverty alleviation (World Bank)—have delivered enormous economic benefits to their founders. Despite occasional challenges, the system has fared well. It has provided stability and market opening, relatively stable foreign exchange rates, the ready availability of capital, and a forum for the coordination of macroeconomic policies. Between the first GATT round in 1947 and the launch of the Doha Round at the WTO in 2001, international trade increased enormously, by more than 100 fold. Global financial flows have grown by a still greater amount. The integration of the world economy

has proceeded apace, propelled by freedom of capital movements, the development of new and expanding markets, economies of scale, cheaper sources of supply of raw materials and finished goods, the international migration of labor, and technological advances in production processes, transportation, and communications.

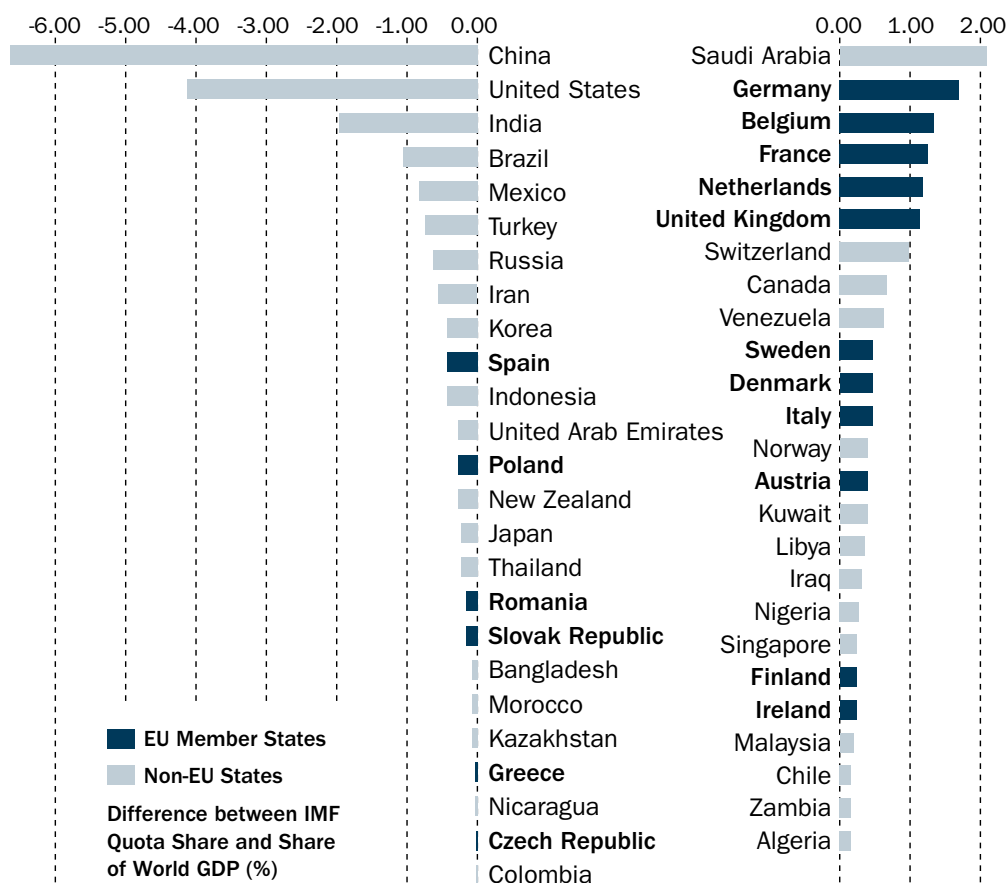
The legacy of this history is that the United States and Europe enjoy outsized control at the Bretton Woods institutions. Both benefit from the unwritten rule that the president of the World Bank is always an American, while the managing director of the IMF is always a European. Seven of the top ten countries that are “overrepresented” at the IMF (in terms of the difference between their IMF quota share and their share of world GDP) are European.

Both the World Bank and the IMF have a board of 24 executive directors, with most of the executive directors speaking for (and voting for) a group of countries. Five countries, however, have their own appointed seats: the United States, Germany, France, the United Kingdom, and Japan. In addition to the German, French, and British seats, the 24 other members of the European Union are part of the group of countries represented by seven other executive directors, thereby giving Europe three exclusive seats and a significant presence in seven others. As such, the EU’s member states can influence 32 percent of the votes at the IMF—and a similar (although not exactly equal) number at the World Bank. At the WTO, the United States and Europe have traditionally made up two of the so-called “quad” countries (the United States, European Union, Canada, and Japan) that for a long time were viewed as the “dealmakers” for any trade agreement, to which the rest of world was expected to simply sign on.

**Figure 1. Under- and over-representation at the International Monetary Fund**

**Under-represented Countries**

**Over-represented Countries**



Notes: 25 IMF members with the smallest and largest differences between IMF quota share and share of world GDP is adjusted for purchasing power parity (PPP).

Source: Rebecca Nelson, "The G20 and International Economic Cooperation: Background and Implications for Congress," Congressional Research Service, Dec. 9, 2009.

# 3 THE GREAT RECESSION AND THE STEERING COMMITTEE OF THE WORLD ECONOMY

*The second major systemic response to the Great Recession has been the transformation of the little-known G20 into the premier forum for international economic cooperation.*

With the bursting of the housing bubble in the United States in 2007 and the train of events that led to the destabilization of the global financial system, the world economy collapsed into a steep recession in the final quarter of 2008, with global real GDP dropping at a 6 percent annual rate. This is undoubtedly the sharpest decline in world output—and especially in world industrial production and world trade—of the postwar era. Worldwide exports plummeted from \$16.1 trillion in 2008 to \$11.2 trillion in 2009, a drop of over 30 percent. Virtually all countries were sucked into the downturn, with the world witnessing the first significant decline in world real GDP (of nearly one percent) in six decades.

The full story of why this collapse occurred is still being written, but it starts with a focus on developments in the United States—especially the expansion and subsequent collapse of the real estate and real estate financing bubble and its impact on an overleveraged U.S. and global financial system. Add to the tale the accounts of persistently easy monetary policies, very low interest rates and interest rate spreads, and a general disregard of growing risks in the financial system, and the key causes begin to come into focus. Others would point to huge current account savings and reserve accumulations in Asia, particularly China, and the mirror-image deficits in the United States as another major underlying cause of the troubles.

This Great Recession of 2008–2009 has tested the international economic institutions as never before. In response, the IMF has stepped up its role as a lender of last resort, providing financial support packages to (among others) Iceland, Ukraine, Hungary, Pakistan, Belarus, Serbia, Armenia, El Salvador, and Latvia, and has also extended credit to Mexico, Poland, and Colombia under a new flexible credit line. In order to better equip the Fund for this task, G20 leaders at their London summit in April 2009 pledged to triple the IMF's

lending capacity to \$750 billion. Additionally, they urged the Fund to intensify its economic surveillance and early warning systems.

The World Bank has also moved to expand and speed up lending, assistance, and advice to developing countries, committing a record high of nearly \$60 billion to countries hit by the financial crisis in fiscal year 2009—an increase of 54 percent over the previous year. An additional \$8.3 billion was mobilized as part of the World Bank's global crisis response initiative to lessen the impact of the crisis on the most vulnerable, especially in low-income countries. These initiatives focus on safety net programs to protect the most vulnerable, maintaining long-term infrastructure investment programs, and on sustaining the potential for private sector-led economic growth and employment creation, particularly through the support of small and medium-size enterprises.

The WTO for its part began a new monitoring and reporting mechanism on protectionist actions taken by WTO members and worked to ensure that markets remained open and that countries adhered to their WTO commitments. The WTO also pushed G20 members to keep their pledges of support for Aid for Trade initiatives and worked to ensure that trade finance remained available and affordable.

The second major systemic response to the Great Recession has been the transformation of the little-known G20 gatherings of finance ministers and central bankers into an affair involving heads of state, declared by these leaders to be “the premier forum for international economic cooperation.”<sup>5</sup> The G20 started in 1999 in the wake of the 1997 Asian financial crisis as a forum that brought together finance ministers from

<sup>5</sup> The Pittsburg Summit: Leaders' Statement, paragraph 19. “We designated the G20 to be the premier forum for our international economic cooperation.”

major advanced and emerging economies with the goal of stabilizing global financial markets. With its ascendancy as part of the response to the Great Recession, it has now supplanted the G7/G8 meetings as the “chief steering committee of the world economy.”<sup>6</sup> The inclusion in the G20 of a number of countries beyond the historical G7/G8 grouping no doubt stemmed, at least in part, from a recognition of the growing power of the emerging market and developing countries, who now account for more than 40 percent of the world economy. To have any sense of legitimacy throughout the world and particularly among the emerging market economies, expansion of the leadership circle was critical.

However, the initial G20 Leaders Summit, held in Washington in November 2008, was something of an EU-U.S. joint venture. British Prime Minister Gordon Brown had been calling for a “Bretton Woods II” to completely revise global economic governance, and the United States responded by promoting the idea of a G20 gathering, elevated to the level of heads of state, and extended the invitation for an initial meeting in Washington. European leaders at first exhibited differences of viewpoint on this approach, with French President Nicolas Sarkozy needing to be convinced of the appropriateness of the G20 as a venue, given that EU member states hold four of the seven seats (57 percent) at the G7 but only those same four seats plus one for the European Union (25 percent) at the G20. But in the end there was acceptance of the G20 as the only available forum with the scope of membership required to develop ideas, reach consensus on their desirability, and work to implement them.

<sup>6</sup> C. Fred Bergsten, Peterson Institute for International Economics, “A Blueprint for Global Leadership in the Twenty-First Century,” Keynote Speech at the Global Human Resources Forum, Seoul, Korea, Nov. 4, 2009.

The evolution of the G20 also caused an evolution in the European approach to such summits. Efforts were made prior to and after each meeting to come to a Europe-wide position, with the European Council adopting a number of principles for action where agreements could be reached—principally in the area of enhancing sound regulation and reforming the international financial institutions. The European Commission was given the task of developing proposals for comprehensive reform of the financial system, which were then endorsed by the European Council and urged upon the rest of the G20 leaders by European heads of state. Throughout these efforts, Europe needed to find common ground among competing positions, with the United Kingdom arguing for more stimulus from other governments, Germany emphasizing the need to avoid major budget deficits, and France pushing for a major clampdown on executive compensation and a general tightening of financial regulation. The United States joined the United Kingdom and Japan in pushing for more stimulus from others while initially resisting any shift of financial regulatory policy out of the hands of national regulators.

What emerged from these G20 summits is fairly remarkable—both in terms of the substance of the consensus that was reached and in terms of the process. Despite starkly differing views on how to stimulate economic growth and recovery, agreement was reached to pump more than \$1 trillion into the global economy—albeit through the IMF, rather than individual countries—in the form of \$500 billion in new lending capacity, \$250 billion in new Special Drawing Rights, and \$250 billion in trade finance. Separately, the G20 asserted that commitments by individual countries for fiscal expansion would total \$5 trillion over two years. Demands from some European countries for a major toughening of the regulation and oversight of financial institutions were met through the creation

*The inclusion in the G20 of a number of countries beyond the historical G7/G8 grouping partly stems from a recognition of the growing power of the emerging market and developing countries, who now account for more than 40 percent of the world economy.*

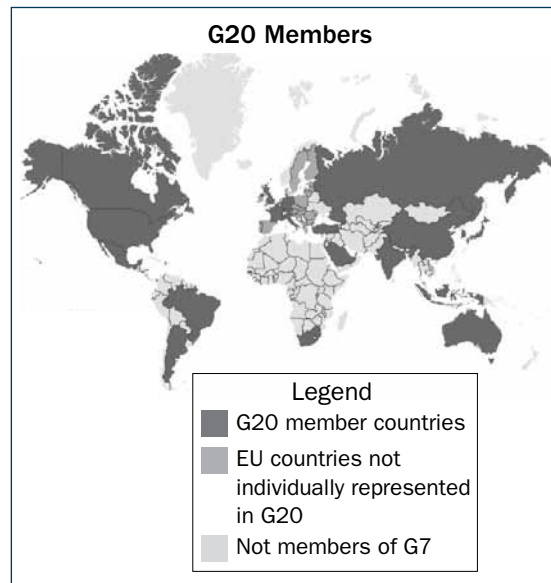
**Table 2. Numbers count: From the G7/G8 to the G20**



Source: G20 website; [www.g20.org](http://www.g20.org)

EU G8: France, Germany, Italy, United Kingdom.

| G7/G8                     |                            |                |
|---------------------------|----------------------------|----------------|
| Country                   | GDP (millions of dollars)* | % of world GDP |
| Canada                    | 1,499,551                  | 2.46%          |
| France                    | 2,866,951                  | 4.71%          |
| Germany                   | 3,673,105                  | 6.03%          |
| Italy                     | 2,313,893                  | 3.80%          |
| Japan                     | 4,910,692                  | 8.06%          |
| United Kingdom            | 2,680,000                  | 4.40%          |
| United States             | 14,441,425                 | 23.71%         |
| <b>G7</b>                 | <b>32,385,617</b>          | <b>53.16%</b>  |
|                           |                            |                |
| Russia                    | 1,676,586                  | 2.75%          |
| <b>G8</b>                 | <b>34,062,203</b>          | <b>55.92%</b>  |
| <b>EU countries in G8</b> | <b>11,533,949</b>          | <b>18.93%</b>  |



Source: G20 website; [www.g20.org](http://www.g20.org)

<sup>1</sup> EU 27: Austria, Belgium, Bulgaria, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Poland, Portugal, Romania, Slovakia, Slovenia, Spain, Sweden, United Kingdom.

<sup>2</sup> Non-G8 EU members: Austria, Belgium, Bulgaria, Cyprus, Czech Republic, Denmark, Estonia, Finland, Greece, Hungary, Ireland, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Poland, Portugal, Romania, Slovakia, Slovenia, Spain, Sweden.

| G20/G20 + non G8 EU                          |                            |                |
|--|----------------------------|----------------|
| Country                                      | GDP (millions of dollars)* | % of world GDP |
| Argentina                                    | 324,767                    | 0.53%          |
| Australia                                    | 1,013,461                  | 1.66%          |
| Brazil                                       | 1,572,839                  | 2.58%          |
| China  | 4,327,448                  | 7.10%          |
| India  | 1,206,684                  | 1.98%          |
| Indonesia                                    | 511,765                    | 0.84%          |
| Mexico                                       | 1,088,128                  | 1.79%          |
| Saudi Arabia                                 | 469,426                    | 0.77%          |
| South Africa                                 | 276,764                    | 0.45%          |
| South Korea                                  | 929,124                    | 1.53%          |
| Turkey                                       | 729,983                    | 1.20%          |
| <b>Subtotal</b>                              | <b>12,450,389</b>          | <b>20.44%</b>  |
| <b>G20 total</b>                             | <b>46,512,592</b>          | <b>76.35%</b>  |
|  |                            |                |
| <b>EU (27)<sup>1</sup></b>                   | <b>18,387,785</b>          | <b>30.18%</b>  |
| <b>G20 + non-G8 EU countries<sup>2</sup></b> | <b>53,366,428</b>          | <b>87.60%</b>  |

\* 2008 GDP

Source: IMF World Economic Outlook Database (Oct. 2009)

of a Financial Stability Board (FSB).<sup>7</sup> The FSB was designed to bring about greater coordination and coverage of regulatory systems to include hedge funds, principles on pay and compensation, controls on excessive bank leverage and bank secrecy, and oversight of accounting standards and credit rating agencies. Those calling for a “Bretton Woods II” and a revamping of the institutions of multilateral economic governance were met at least halfway: there was eventual agreement on the U.S. proposal to increase the IMF quota share of the emerging market countries by five percentage points, along with an increase in the voting power of developing and transition countries at the World Bank of at least three percent and a commitment to reform the “mandates, scope and governance” of

---

<sup>7</sup> The Financial Stability Board was established at the London G20 Summit as a successor to the Financial Stability Forum, which was created in 1999 by the G7 finance ministers and central bankers as a forum to promote coordination and information exchange among those responsible for financial stability. The FSF was made up of financial regulators from the G7 countries, Australia, Hong Kong, Netherlands, Singapore, and Switzerland, as well as international financial institutions, international regulatory and supervisory groupings, committees of central bank experts and the European Central Bank. When the G20 leaders transformed the FSF into the FSB, they expanded its membership to include 64 participants—all G20 countries, plus Hong Kong SAR, the Netherlands, Singapore, Spain, Switzerland, the European Central Bank, and the European Commission. They also significantly expanded its mandate to include assessments of vulnerabilities in the financial system, monitoring market developments, advising on best practices in meeting regulatory standards and the establishment of guidelines and support for supervisory colleges. U.S. Treasury Secretary Timothy Geithner described the FSB as “a fourth pillar to the architecture of cooperation established after the second world war” referring to the IMF, the World Bank and the WTO, noting his expectation that the FSB will set high global financial standards and hold all FSB members accountable to those standards.

the financial institutions, while Europe’s desire to keep the number of seats on the Executive Boards of the IMF and the World Bank at 24 was met. The WTO was included in the later G20 meetings, and was given the task of monitoring G20 pledges not to take any protectionist action and to complete the Doha Round of trade negotiations.<sup>8</sup>

A pattern began to emerge from the G20 summits whereby the heads of state would assign tasks to the multilateral economic institutions related to specific issues, with instructions to report back to the next meeting of G20 leaders. While the response to the initial Washington summit was not impressive, with markets around the world falling significantly after its conclusion, as the actions by the multilateral institutions and governments to carry out their assigned tasks started to take shape, the reaction to the subsequent summits was much more positive. Also of interest is the emerging process by which disagreements among, for example, major European players like Germany, France, and the United Kingdom, or between Europe and the United States, were brokered by other G20 members, with India or China or Brazil serving this role of referee and conciliator.

---

<sup>8</sup> The WTO’s scarce resources and prescribed impartiality places strong constraints on its ability to effectively name and shame members for adopting protectionist measures. A number of independent monitors, most prominently Global Trade Alert (GTA), [www.globaltradealert.org](http://www.globaltradealert.org), have stepped in to analyze protectionist measures using a much broader definition of what constitutes a protectionist action. With regard to the G20 pledge to “refrain from raising new barriers to investment or to trade in goods and services,” GTA found that, “on average, a G20 member had broken the no-protectionism pledge every three days” in the year following the Washington Leaders Summit.



**Table 3. G20 leaders summits: Pledges and commitments**

| G20 Leaders Summits               | Pledges/Commitments   |
|-----------------------------------|---|
| <b>Washington, November 2008</b>  | <ul style="list-style-type: none"> <li>• Adopted 5 principles for reform relating to transparency, accountability, and enhanced regulation of financial markets, products, and participants, including credit rating agencies, with an action plan for their implementation</li> <li>• Pledged to coordinate regulatory reforms internationally</li> <li>• Committed to reform Bretton Woods Institutions to reflect changed economic weights in the world economy, but no specifics</li> <li>• Pledged to use expansionary macroeconomic policies, both fiscal and monetary, to stimulate aggregate demand and encourage economic growth</li> <li>• Committed to refrain from protectionist trade policies and to “strive” to reach agreement on the Doha Round of WTO talks.</li> </ul>   |
| <b>London, April 2009</b>         | <ul style="list-style-type: none"> <li>• Reiterated commitments of 2008</li> <li>• Creation of Financial Stability Board (FSB) as successor to Financial Stability Forum with all G20 countries, FSF members, Spain and the European Commission as FSB members, set up to establish and enforce high global standards for financial regulation and monitoring</li> <li>• IMF: Pledge to increase funding for the IMF and MDBs by \$ 1.1 trillion, including a tripling of the IMF's lending capacity by restocking the IMF with \$500 billion and creating \$250 billion of new Special Drawing Rights.</li> <li>• World Bank: support for increase in lending of at least \$100 billion and implementation of 2008 reforms</li> <li>• Commitment to conclude an “ambitious” Doha Round and to avoid protectionist measures</li> </ul>  |
| <b>Pittsburgh, September 2009</b> | <ul style="list-style-type: none"> <li>• Agreed on a “Framework for Strong, Sustainable and Balanced Growth” to coordinate and monitor national economic policies to correct the current global imbalances and prevent future such imbalances, with some peer review and some IMF oversight of this macroeconomic policy coordination</li> <li>• Specific plans to increase the representation of emerging-market countries at the IMF by increasing their quota by five percentage points to 43% of the total and similar initiatives at the World Bank</li> <li>• Commitment to crack down on financial institution excesses, including raising capital standards, implementing international compensation standards and adopting frameworks for cross-border resolutions of failed institutions</li> <li>• Commitment to conclude the Doha Round by the end of 2010</li> </ul> |
| <b>Participants</b>               | <p><b>Washington:</b> Argentina, Australia, Brazil, Canada, China, France<sup>1</sup>, Germany, India, Indonesia, Italy, Japan, Mexico, the Netherlands<sup>2</sup>, Rep. of Korea, Russia, Saudi Arabia, South Africa, Spain<sup>2</sup>, Turkey, United Kingdom, United States</p> <p>Ex-officio participants: European Commission (President), World Bank (President), Secretary General of the UN, IMF (Managing Director), Financial Stability Forum (Chairman)</p> <p><b>London:</b> All Washington participants plus Czech Republic<sup>3</sup> and ex-officio participants: Chair of New Partnership for Africa's Development (NEPAD), Chair of Association of Southeast Asian Nations (ASEAN), WTO (Director-General)</p> <p><b>Pittsburgh:</b> All participants from London with Sweden<sup>3</sup> representing the EU Council rather than the Czech Republic</p>      |

<sup>1</sup> Representing EU Council and themselves

<sup>2</sup> Permitted extraordinary presence

<sup>3</sup> Representing the EU Council

Source: G20 website, [www.g20.org](http://www.g20.org)

# 4 THE IMF, WORLD BANK, AND WTO: FROM CRISIS TO REFORM

With each successive wave of economic crisis to hit the world—from the Asian meltdowns in 1997 to Russia's ruble crisis in 1998 to the collapse of Argentina in 1999 and 2000—there has been a subsequent torrent of hand-wringing, post-mortem analysis, and calls for reforms to the architecture of global economic governance in order to speed recovery and prevent such crises from reoccurring. Equally compelling has been a wave of tragedies—from the tsunami in the Indian Ocean to Hurricane Katrina in 2005 to the enduring poverty throughout much of Africa—that have tested the world's ability to respond, accompanied by calls for a better approach to development contained in many a bestselling book or prominent commission report. On the trade front, the WTO took center stage not long after its creation, when protestors outnumbered delegates at its Ministerial meeting in Seattle in 1999, setting a precedent for civil disturbances at meetings of the WTO, IMF, and World Bank ever since. Overall, the clamoring for reform reached a crescendo with the Great Recession of 2008-2009, which has prompted a number of pledges from political leaders to learn from the mistakes of the past and to reform the global economic architecture to meet the challenges of the 21st century.

The various calls for reform have pin-pointed problems of relevance, effectiveness, and legitimacy. Waning *relevance* in the case of the IMF has been detected as a result of the ascendance of private capital markets; at the World Bank, as a result of the rise of China and other new economic powers engaging in infrastructure development; and at the WTO as a result of the proliferation of regional trade agreements. Waning *effectiveness* at the IMF is a claim directed at the Fund's inability to tackle global imbalances and its "mission creep" into bailouts; at the World Bank it has been identified in relation to the inability substantially

to improve poverty rates, particularly in Africa, or adequately address environmental, human rights or corruption concerns, along with a perceived "mission creep;" and at the WTO it has arisen from the inability to conclude the Doha Round despite the nine years that have lapsed since talks began in November 2001. Finally, waning *legitimacy* has been diagnosed at both the IMF and the World Bank as a result of the lack of voting power or quota levels held by emerging and developing countries and the perception that the institutions are controlled by a handful of wealthy countries that impose conditionality on others but not themselves; at the WTO, it arises from a perceived lack of transparency in its operations combined with concerns that the consensus-only decision making process may be getting in way of reaching conclusions, and from a longstanding failure to ensure that the benefits of free trade are more evenly distributed.<sup>9</sup>

<sup>9</sup> Much work on reform proposals had been done well before the G20 Summits. See, for example, World Trade Organization (2004), *The Future of the WTO: Addressing Institutional Challenges in the New Millennium: Report of the Consultation Board to the Director-General Supachia Pantichpakdi* (the "Sutherland Report"); and the report of the IMF's Independent Evaluation Office, *Governance of the IMF: An Evaluation*, 2008. In addition to the work of such commissions, there have been countless books and articles written, many of which are noted in the bibliography at the end of this article. Key among them would be *Losing the Global Development War*, John W. Heard, 2008; *Reforming the IMF for the 21st Century*, Edwin M. Truman, 2006; *Redesigning the World Trade Organization for the 21st Century*, Debra P. Steger (2010); *Studies of IMF Governance*, Ruben Lamdany and Leonardo Diaz Martinez (2009); *The IMF and its Critics*, (2004) and *The World Bank: Structure and Policies* (2000) David Vines and Christopher Gilbert; "Reforming the World Bank," Jessica Einhorn, *Foreign Affairs*, Jan./Feb. 2006, Vol. 85, Issue 1, and *The IMF, World Bank and Policy Reform*, Alberto Paloni and Maurizio Zanardi, Routledge Studies in Development Economics, 2006. In addition, a number of groups have been formed devoted to reform of these institutions, including The Bretton Woods Project ([www.brettonwoodsproject.org](http://www.brettonwoodsproject.org)), New Rules for Global Finance Coalition ([www.new-rules.org](http://www.new-rules.org)) and The Fourth Pillar ([www.fourthpillar.org](http://www.fourthpillar.org)).

*The various calls for reform have focused on a perceived lack of relevance, effectiveness, and legitimacy at the IMF, the World Bank, and the WTO.*



It is in the face of these challenges that G20 leaders have called for reforms to the international financial institutions. These reforms will primarily focus on changes to their mandates, scope, and governance to reflect the increasing complexity in the world and changes in the economic weight of the various players. In addition, the reforms will also involve greater coordination and coherence among the three economic institutions, along with the newly created Financial Stability Board.

Implicit in various calls for reform is a reaffirmation of support by the G20 leaders for a multilateral approach to economic problems and for increased reliance on the multilateral economic institutions to help solve them. Such increases will necessarily also involve finding a way to “multilateralize” many of the existing regional agreements that cut into the scope of the work of these institutions. Equally implicit in the G20 leaders’ statements is support for the ongoing work of these existing institutions of global economic governance.

*In the wake of the Second World War, it was America that largely built a system of international institutions that carried us through the Cold War. Leaders like Harry Truman and George Marshall knew that instead of constraining our power, these institutions magnified it.*

*Today it's become fashionable to disparage the United Nations, the World Bank, and other international organizations. In fact, reform of these bodies is urgently needed if they are to keep pace with the fast-moving threats we face. Such real reform will not come, however, by dismissing the value of these institutions, or by bullying other countries to ratify changes we have drafted in isolation. Real reform will come because we convince others that they too have a stake in change—that such reforms will make their world, and not just ours, more secure.*

*Then-presidential candidate Barack Obama  
The Chicago Council on Global Affairs  
April 23, 2007*

# 5 GUARDIAN OF GLOBAL FINANCE: THE INTERNATIONAL MONETARY FUND

## Mission

The principal international institution involved in financial stability and finance matters is the International Monetary Fund. The Fund has evolved considerably from its original role, which focused on management of the par value system of fixed exchange rates. When the United States eliminated adherence to the gold standard and the system of pegged exchange rates in 1971, countries were left free to choose their exchange rate regimes and the IMF's charter was radically amended, pushing it to focus heavily on member countries with persistent balance-of-payment problems and on responding to crises that threaten the international monetary system as a whole. The Fund's scope was also fundamentally altered by the emergence of newly independent nations in Africa and elsewhere beginning in the late 1950s, followed by another wave of new entrants after the end of the Cold War, both of which required a change in financing and policy advice to support growth-oriented structural reforms and transitions from centrally-planned to market economies. The IMF currently carries out its mission through a combination of financing (typically done through stand-by arrangements or special loans), surveillance of countries' economic and financial policies, technical assistance, and policy endorsements.

## Governance

Both the IMF and the World Bank have a Board of Governors made up of a representative of all 186 countries which meets twice a year. The IMF's Board of Governors is advised by two ministerial committees, the International Monetary and Financial Committee (IMFC), and the Development Committee. While some specific powers reside with the Board, the real management of the IMF is done by its Executive Board of 24 members, five of whom are appointed

(the United States, Japan, Germany, France, and the United Kingdom), three of whom are elected by a single country (China, Russia, and Saudi Arabia), and 16 of whom are elected to represent a group of countries, along with the managing director of the IMF, who serves as the chairman of the Executive Board.<sup>10</sup> Over and above the appointees of Germany, France, and the United Kingdom, the remaining members of the European Union are all represented on the Executive Board in one of seven different country groupings. Each member of the Executive Board controls a share of the total vote at the IMF, depending on the size and level of participation of those countries in his or her group. The United States has the largest single voting share with 16.77 percent, followed by Japan (6.02 percent), Germany (5.88 percent), France (4.85 percent), and the United Kingdom (4.85 percent). While many decisions at the Executive Board are made on the basis of majority rule, some key decisions require a super-majority vote of 85 percent, which gives the United States, with its 16.77 percent share, the ability to block such decisions. If the three appointed European representatives voted together, they too would have more than 15 percent of the vote and would have, like the United States, enough power to "veto" any action that required a supermajority vote of 85 percent. While the IMF's quota shares are automatically updated, these updates have not resulted in a substantial shift in power away from overrepresented Europe to underrepresented emerging market economies.

With respect to recent governance reform efforts at the Fund, Managing Director Dominique Strauss-Kahn created a "four pillar" approach to reform, calling for a report from the IMF's Independent Evaluation Office, from an internal Working Group

<sup>10</sup> Including the managing director, there are currently 10 Europeans (40 percent of the total) serving on the IMF's Executive Board.

*Dissatisfaction with Fund governance well pre-dates the crisis, reflecting a sense of declining relevance (given ascendant private capital markets), effectiveness (demonstrated by the Fund's inability to tackle global imbalances), and legitimacy (with institutional structures described as outmoded and feudalistic).*

on IMF Corporate Governance, from civil society organizations, and lastly from the Committee on IMF Governance Reform headed by South African Finance Minister Trevor Manuel. As the Fund's internal report noted, "dissatisfaction with Fund governance well pre-dates the crisis," reflecting a sense of waning relevance (given ascendant private capital markets), effectiveness (demonstrated by the Fund's inability to tackle global imbalances), and legitimacy (with institutional structures described as "outmoded and feudalistic").<sup>11</sup>

In attempting to address at least the concerns about relevance and legitimacy, the Manuel Committee was established in September 2008 and issued its report on March 25, 2009, in advance of the spring meeting of the IMF. The Committee's report called for:

- The creation of a high-level ministerial council (IMF Council) to foster political engagement in strategic and critical decisions;
- An acceleration of the quota and voice reform begun in 2009 by shifting to a 70 to 75 percent majority for decisions, which would have the effect of removing the U.S. veto power while giving low income countries the ability to band together to veto activities they do not like;
- A broader mandate for surveillance to include macroeconomic policies, prudential issues, and financial spillovers;
- Clearer lines of responsibility and accountability among various decision-making entities in the Fund with more authority for member-specific surveillance given to management and greater strategic and supervisory roles for the Executive Board; and

- The introduction of an open, transparent, and independent-of-nationality selection process for the Managing Director, thereby eliminating the unwritten rule that the Managing Director must be a European.

For its part, the Independent Evaluation Office report, *Governance of the IMF*, recommended:

- Clarification and alteration of the roles and responsibilities within the IMF governance structure to minimize overlaps and close gaps;
- Active and systematic ministerial-level involvement in setting strategic goals and overseeing performance;
- Reorientation of the Board away from executive functions to a supervisory role focused on formulating strategy, monitoring policy implementation, and exercising executive oversight; and
- Establishment of a framework to hold management accountable for its performance.

Civil society organizations, for their part, emphasized through their "fourth pillar" process a greater need for transparency and communication, particularly with the executive directors, along with strong calls for changes to the distribution of voting power and quotas and increased accountability for the executive board. They also insisted that the selection of the managing director and the deputies should be conducted via a merit-based, transparent process without any restrictions as to the nationality of the candidates.

### **Mandate**

With respect to the mandate of the IMF, the current economic crisis has pointed to the need for a number of substantial changes to the mandate of the IMF. These include the establishment of a

<sup>11</sup> International Monetary Fund, "IMF Governance—Summary of Issues and Reform Options", Strategy Policy, and Review Department and the Legal Department, Jul. 1, 2009.

sound early warning system for macroeconomic and financial risks, broader surveillance of all members' macroeconomic policies (including the United States and European Union member states), tougher oversight of exchange rate imbalances,

and broad-based support for growth in developing countries by helping finance counter-cyclical spending, bank recapitalization, infrastructure, trade finance, balance of payments support, debt rollover, and social support.

# 6 FROM RECONSTRUCTION TO DEVELOPMENT: THE WORLD BANK

*Europe has long favored a World Bank focused almost exclusively on poverty alleviation, while the U.S. wants additional emphasis placed on private sector engagement and development.*

## Mission

Among the multilateral institutions, the task of promoting global development and poverty alleviation primarily falls to the World Bank. The World Bank has evolved from its inception as an institution with 44 member countries and a focus on postwar reconstruction to a development services organization with more than 10,000 employees and an administrative budget of \$1.6 billion. Last year, its loan commitments totaled \$46.9 billion. Over the years, its core focus has shifted from growth through trade and investment in partnership with middle-income countries to an organization set on alleviating poverty and promoting development in poor countries.

In the main, the United States and Europe have had shared goals for and commitment to the work of the World Bank Group. However, historically there have been some differences in approach. At its inception, the United States saw the Bank as responsible for building a strong middle-class and overall economic prosperity in middle-income countries, in part to provide markets for U.S. exports. As the Bank moved from reconstruction to a focus on development, the United States has typically favored a mission that continues to place strong emphasis on the pursuit of economic growth and productive investment that leans heavily on the private sector. Europe was initially on the receiving end of the Bank's reconstruction efforts, until much of that work was taken over by the Marshall Plan. Once fully recovered, Europe began to push for the Bank to work almost exclusively with the poorest countries and the poorest pockets of the middle-income countries, and the Europeans remain strong proponents of this primary focus on poverty alleviation.

## Governance

The governance structure of the World Bank largely mirrors the structure of the IMF, with a Board of Governors that meets twice a year and the real management of the Bank done by its Executive Boards, which are also composed of 24 directors who are appointed or elected by the same member countries or groups of countries as the IMF along with the president of the Bank, who serves as its chairman.<sup>12</sup> The voting weight of each country is made up of both basic votes (whose value has eroded over time) and votes that are dependent on a country's shareholding in the Bank. Unlike at the IMF, which has automatic quota reviews every five years, shareholding adjustments are made through periodic—and generally very political—processes. With 16.4 percent, the United States has by far the largest voting weight at the Executive Board of the International Bank for Reconstruction and Development, followed by Japan (7.87 percent), Germany (4.49 percent), France (4.31 percent), and the United Kingdom (4.31 percent). These five countries have the right to appoint their own representatives to all four Executive Boards. Three other countries elect a single representative to each of the Executive Boards (China, Russia and Saudi Arabia), while the remaining 16 directors are elected to represent a group of countries. As with the IMF, all of the other members of the European Union participate as part of a group of countries represented by one of seven other elected representatives on the Executive Board.

Decisions at the Bank are made by simple majority vote for ordinary decisions and by supermajority (85 percent) for one type of decision—amendments to the Article of Agreement. As at the IMF, because

<sup>12</sup> Technically the World Bank Group has four boards (IBRD, IDA, IFC, and MIGA) of executive directors with slightly different voting percentages for each, but as a practical matter, the same individual typically serves as the executive director on all four.

| Table 4. The World Bank Group today                        |      |  |   |  |
|--|------|--|---|--|
| World Bank Group   | Est. | Areas of specialization  | Cumulative Lending/<br>commitments<br>(billions)                                    | Fiscal 2009 Lending/<br>commitments<br>(billions)                    |
| International Bank for Reconstruction and Development      | 1944 | Focuses on lending to public sector entities in poor to middle income countries.   | \$479<br>(effective FY 2005, includes guarantees)                                   | \$32.9 for 126 new operations in 42 countries                        |
| International Development Association                      | 1960 | IDA lends to world's poorest countries. Provides interest-free loans and grants to public sector to boost growth and reduce inequality. Major source of financing for infrastructure.  | \$207<br>(effective FY 2005, includes guarantees)                                   | \$14 for 176 new operations in 63 countries                          |
| International Finance Corporation                          | 1956 | Finances private sector investment, mobilizing capital in financial markets, and providing advisory services to businesses. IFC invests in enterprises majority-owned by the private sector. Aims to address constraints to private sector investment in infrastructure, health, and education.          | \$34.4 (plus \$8 in syndicated loans)   | \$10.5 committed and \$4 mobilized for 447 projects in 103 countries |
| Multilateral Investment Guarantee Agency                   | 1988 | Promotes FDI into developing countries by providing political risk insurance (guarantees) to the private sector. Insures investment against losses related to expropriation, currency transfer restrictions, civil disturbance/war, breach of contract, non-honoring of sovereign financial obligations. | \$20.9<br>(includes amounts leveraged through the Cooperative Underwriting Program) | \$1.4 in guarantees issued for 26 projects                           |
| International Centre for Settlement of Investment Disputes | 1966 | Autonomous international institution aims to provide facilities for conciliation and arbitration of international investment disputes.   | 292 cases registered  | 24 cases registered in 2009  |

The term "World Bank" typically refers only to the IBRD and IDA. The World Bank Group also encompasses the IFC, MIGA, and ICSID.

Source: World Bank Annual Report 2009.

*In October 2008, World Bank President Zoellick established a high-level commission to focus on the modernization of World Bank Group governance so the World Bank Group can operate more dynamically, effectively, efficiently, and legitimately in a transformed global political economy.*

the United States controls more than 15 percent of the vote, it alone has an effective “veto” power to block any such changes to the Article, and a mythology has ballooned around the perceived reach of this veto power.

Many proposals for governance reform at the World Bank have been made over the years, primarily aimed at addressing the various imbalances that result from the appointed seats held by the “big three” European countries, or from the U.S. “veto” power. Most recently, in October 2008, World Bank President Robert Zoellick established a high-level commission, headed by former Mexican President Ernesto Zedillo, to “focus on the modernization of World Bank Group governance so the World Bank Group can operate more dynamically, effectively, efficiently, and legitimately in a transformed global political economy.”

At the outset, the Commission on Modernization of World Bank Group Governance noted significant weaknesses in three key areas of the Bank’s decision making and governance processes: strategy formulation, voice and participation, and accountability.

On *strategy formulation*, the Commission found that the Bank lacks an effective means to formulate a clear strategy that can be used to set priorities, balance tradeoffs, and align operations and resources with strategic goals. In part, this is due to the advisory nature of the Development Committee and the insufficient time available to—and seniority among—the members of the Bank’s current Executive Board.

On *voice and participation*, the Commission noted that the decision-making process is widely seen as too exclusive and that a number of conventions and practices create the perception that the Bank is accountable and responsive to at best only a handful of shareholders. Contributing to this

perception is the significant gap between the voting shares of developing versus developed countries, an allocation of voting power and special majority rules that gives rise to the “U.S. veto” and the considerable overrepresentation of European countries on the Bank’s Executive Boards.

On *accountability*, the Commission cited in particular the ambiguous relationship between the Board and management, the conflict of interest from the president of the Bank also serving as the chairman of the Executive Boards, the difficulty in holding the president accountable for performance, and the non-transparent process for the selection of the president, with its unwritten convention that the president of the Bank must be a U.S. citizen (just as the managing director of the IMF must be a European).

The Zedillo Commission issued its report in October 2009, which included five recommendations that the Commission noted need to be adopted and implemented as a single package:

- *Enhancing voice and participation* by consolidating the board to 20 chairs from the current 24, composing the board entirely of elected chairs that represent multi-country constituencies, and eliminating the link between the IMF quotas and the World Bank voting powers;
- *Restructuring the World Bank’s governing bodies* by elevating the Board to ministerial level with responsibility for overall strategy and direction, major policy decisions, oversight and selection of the President, delegating to management the approval of financing operations and creating an advisory council of representatives;
- *Reforming the leadership selection process* by creating a rules-based, inclusive, competitive process for selecting the President that does



away with the current un-written rule that reserves the Bank presidency to a U.S. citizen;

- *Strengthening management accountability* by creating a performance review process for the Bank president, increasing use of external evaluations and increasing reviews of those providing safety nets for the poorest; and
- *Strengthen the Bank's resource base* through increases to its capital base.

### Mandate

With respect to the mandate of the World Bank, significant change has already occurred. However, as the many calls for reform indicate, much remains to be done. With four branches in addition to the original International Bank for Reconstruction and Development and the establishment of regional development banks, the World Bank has moved far beyond its initial role of lending to public-sector entities for reconstruction. Much of the World Bank's current support is provided through equity investments, financial services, and political risk insurance, in addition to traditional lending and project financing.

In today's world, it is clear that more needs to be done to broaden and deepen the role of the Bank, particularly in its relationships with non-state actors, be they private business, NGOs, or bilateral aid donors, as central components of its development strategy and to ensure that it is not trying to be all things to all people. Global leaders and scholars alike have noted that the path to economic recovery is one that will be primarily paved by the private sector, be it small and large businesses, entrepreneurs, microfinance lending groups, or risk-takers and financiers from around the world.

Private sector growth has been the engine that allowed hundreds of millions of people to lift themselves out of poverty in China and India in recent decades. From Dambisa Moyo's notion, in *Dead Aid*, that development assistance to governments is "easy money" that furthers poor governance and adds to the poverty of Africa rather than helping it, to R. Glenn Hubbard and William Duggan's call, in *The Aid Trap*, for a new Marshall Plan of lending directly to private enterprises in the world's poorest nations, to the inclusion of a global partnership for development with the private sector as part of the Millennium Development Goals, there are growing calls for more resources to be directly granted to private and local business in order to both cultivate a middle class and to place market incentives and disciplines on more economic activity. In addition, the Bank needs to adjust its approach to address the considerable competition it now faces in the development of infrastructure from countries, particularly China, who are willing to invest directly in large-scale projects without many of the policy strings ("conditionality") normally attached by the Bank to those activities. It also needs to ensure that the Bank is playing as big a role as possible in the effort to ensure that development and sustainable economic activity go hand in hand. Moreover, the G20 has conferred on the Bank a leading role in responding to problems requiring "globally coordinated action, such as climate change and food security."<sup>13</sup>

---

<sup>13</sup> Pittsburgh Summit, Leaders' Statement, September 24-25, 2009, paragraph 21.



# 7 NEGOTIATING THE RULES: THE WORLD TRADE ORGANIZATION

## Mission

As with the IMF and the World Bank, the principal governing institution of the global trading system—first the General Agreement on Tariffs and Trade, then its successor, the World Trade Organization—has undergone major changes since it was first conceived in the 1940s. Following the failure of the United States to ratify the Havana Charter that would have created the International Trade Organization, a smaller group of 23 countries joined together in a looser arrangement to provide reciprocal tariff reductions and to agree to certain codes governing their trading relationships. The GATT provided the forum in which eight rounds of multilateral trade negotiations were completed, substantially lowering tariffs on industrial goods among industrial countries (although not yet in agricultural products or the labor-intensive manufactured goods of export interest to many developing countries). Through its system of tariff bindings, transparency, and adherence to rules—especially the principle of nondiscrimination expressed in the *most favored nation* (MFN) and *national treatment* provisions—the GATT also provided an underpinning of institutional stability and predictability in international trade that served as a guarantor against the threat of 1930s-style protectionism throughout the second half of the 20th century.

With the increasing complexity of global commerce came the recognition among GATT members of the need for an organization that could provide more comprehensive regulation of international trade. The ITO as it was originally envisioned would have held a wide remit beyond trade in goods, with the ability to negotiate rules governing labor standards, commodity agreements, restrictive business practices, international investment, and trade in services. With the conclusion of the Uruguay Round negotiations, the GATT membership agreed to the launch, in 1995, of a full-fledged

international organization, the World Trade Organization, which now has a membership of 153 countries. As with the original ITO, the WTO is concerned with disciplines on trade beyond just goods, and covers trade in agriculture and services as well as rules on intellectual property, subsidies, investment, and trade facilitation. The WTO also boasts a binding dispute settlement mechanism.

## Governance

Unlike the Bank and the Fund, the WTO does not have a formal governance structure with a governing or executive board. Instead, the WTO is a member-driven institution, run by its members with a relatively small secretariat that has very limited power to propose, much less to impose, solutions to problems. It is organized through a series of councils—primarily the General Council, the Dispute Settlement Body, and the Trade Policy Review Body, along with the Council for Trade in Goods, the Council for Trade in Services, and the Council for Trade-Related Aspects of Intellectual Property Rights—which are chaired by a Geneva representative of a WTO member country with an annual rotation of the chairs. In addition, there are numerous committees and working parties on particular issues that are open to all members. While the agreement establishing the WTO set forth a number of procedures by which votes could be taken on certain issues, in practice the WTO has continued to operate on a consensus basis.

Cries for reform of the WTO began in earnest following the huge protests and failure to reach agreement at the WTO's infamous 1999 Ministerial Conference in Seattle, Washington. Four years later, shortly before another less-than-successful Ministerial Conference in Cancún, the then-Director General of the WTO, Supachai Panitchpakdi, established a consultative board to address the future of the WTO and the institutional challenges it faced. That group, led by former WTO

Director General Peter Sutherland, issued its report in December 2005, on the tenth anniversary of the creation of WTO.

Among other things, the Sutherland Report focused on the consensus-based decision-making process. It recommended that more onus be placed on any member blocking a measure that otherwise enjoys strong consensus, and that the WTO re-examine the principle of plurilateral approaches to negotiations and the possibility of approving decisions by a critical mass of members. Also recommended were regular annual ministerial meetings, a WTO Summit of world leaders every five years, and the establishment of a consultative body for senior officials that would meet on a quarterly basis. It urged the development of a set of objectives for the WTO's relations with civil society and the public at large. The report also expressed deep concerns about the spread of regional *preferential trade agreements* and called for such agreements to be subject to meaningful review and effective disciplines at the WTO.

Two years later, Warwick University in the United Kingdom established its first Warwick Commission with a broad mandate to examine the governance of the multilateral trading system in light of growing challenges. The Commission looked at ways to counter growing opposition to further trade liberalization in industrialized countries and to ensure that the end of the dual domination of the trade regime by the United States and Europe does not give way to long-term stalemate or disengagement. It sought ways to forge a broad-based agreement about the WTO's objectives and functions and to ensure that the WTO's many agreements result in benefits for its weakest members. Finally, as with the Sutherland Report, it looked at ways to ensure that the proliferation of regional preferential trade agreements does not undermine the WTO principles of nondiscrimination and transparency in

international commerce. Among other things, the Warwick Commission recommended a *critical mass* approach to decision-making and urged that the industrialized countries refrain from negotiating preferential agreements with each other as well as the development of WTO disciplines and review mechanisms for such agreements. At its most recent Ministerial Conference in December 2009, in the face of the continued inability to conclude the Doha Development Round of trade talks, more than 20 countries endorsed a proposal to establish a process to review the WTO's "functioning, efficiency, and transparency, and consider possible improvements" in light of the "rapid change in the global economic environment" and the need for the WTO to be "agile and responsive." To date, none of these calls for reform have resulted in any changes in the WTO's governance structure.

### Mandate

The WTO is still wrestling with the new mandate it was given in the transition from the GATT to an institution with a scope that was closer to that of the original ITO. Already a chorus of voices—including that of the European Union—is calling for a still-further broadening of the WTO's mandate, with some attributing the failure to conclude the Doha Round in part on its narrow agenda of "yesterday's issues"—namely, market access in agriculture, in goods, and in services.<sup>14</sup> Other WTO members like Brazil and South Africa are more resistant, refusing to move on to new issues until developed country members make good on a promise that was made at the end of

<sup>14</sup> See for example, Aaditya Mattoo and Arvind Subramanian, "From Doha to the Next Bretton Woods, A New Multilateral Trade Agenda," *Foreign Affairs*, Jan./Feb. 2009, contending that a new round of talks is needed to develop a more ambitious agenda than Doha, involving a broader set of institutions than just the WTO and focusing on a wider array of issues, including food security (export bans on agriculture, biofuels policies, etc), cartels, energy trade, exchange rates, regulation of sovereign wealth funds, and climate change.

*Already a chorus of voices—including that of the European Union—is calling for a still-further broadening of the WTO's mandate, with some attributing the failure to conclude the Doha Round in part on its narrow agenda of "yesterday's issues"—namely, market access in agriculture, in goods, and in services.*

the Uruguay Round—that, after a half-century of resistance, liberalization would be extended to trade in farm products and in light manufactures of export interest to developing countries. This long-running standoff is at the heart of the present deadlock in the Doha Round.

However these issues find resolution, it is clear that if the WTO is to remain relevant it will need to be engaged in the trade issues, broadly defined, of the

twenty-first century. These include competition policy, investment policy, energy policy, food security, global health services, technology, environmental goods and services, and a host of additional issues that are both contentious and at the core of business concerns—including corruption, corporate social responsibility, exchange rates, immigration, and cyber security.

# 8 RENOVATING THE HOUSE OF GLOBAL ECONOMIC GOVERNANCE FOR THE 21ST CENTURY

A number of obvious commonalities and themes stand out from these various calls for reform of the Bretton Woods architecture:

- All recognize that the institutions of global economic governance were created at a very different time and under very different circumstances but have failed to change, particularly with respect to the changing distribution of economic weight and power among nations;
- All recognize that the imperative for change must come from political leaders who are above any particular institution in recognition of the fact that it is virtually impossible to change governance structures from within, particularly when such changes involve shifting power away from some to others;
- All call for increased and active involvement at higher political levels in the governance of the institutions, particularly in setting strategic direction; and
- All support a broadening or deepening of the range of activities and mandates of the existing institutions.

It remains to be seen whether the sheer imperative for a coordinated global response to the financial crisis and the emergence of a broader and stronger consensus among the G20 leaders will provide the needed catalyst for change, or whether these blueprints for reform will join a long line of well-

thought-out proposals issued with varying degrees of fanfare only to sink without trace in the ocean of well-meaning but failed ideas, swept away by many of the same forces that make it harder to reach international consensus on anything. However this may be, in the meantime it is a source of hope that the change that is most needed is not impossible to achieve. For the multilateral economic institutions do not need to be completely reconstructed from the ground up. That would be unrealistic. The current crisis is unlikely to be either deep enough or of sufficient duration to create a “1944 moment”—a constitution-making moment when major new institutions and institutional relationships can be built anew or created out of whole cloth. Instead, what is most needed is more akin to a *renovation* and not a rebuilding.

This renovation of the house of global economic governance would involve a rebalancing of power within the existing institutions away from Europe and the United States and toward the rest of the world. It would involve a broadening of the mandates of these institutions to enable them to address the new issues of the day. It would mean a deepening of the coordination among the institutions, including the WTO, to ensure that pressing issues do not fall between the cracks. Finally, it would mean a new commitment on the part of the major players to work to bring the proliferation of regional agreements on the sidelines into their folds.

How can this be done?

*This renovation of the house of global economic governance would involve: a rebalancing of power, a broadening of mandates, a deepening of coordination, and a commitment to bring regional agreements into the fold.*

## 9 THE HARBINGER OF GLOBAL GOVERNANCE: POLITICAL LEADERSHIP AND THE G20

*Use of the G20 as a “Council of Governors” would give the emerging market countries a permanent and significant voice in global economic governance, getting them more engaged in addressing problems at the multilateral level and allowing them to play an important brokering role when differences between the United States and Europe threaten to cause global gridlock.*

The simplest way to achieve these goals is to transform the G20 into a “Council of Governors” for the three established international economic institutions plus the new Financial Stability Board. While the G20 may not be perfect—and debate will doubtless continue as to whether the current configuration is the optimal one—the fact is that it has defied its doubters in reaching consensus on specific approaches to a number of critical and controversial issues. Both the United States and Europe emerged from the three summits with a good deal of confidence in the grouping. “When we are talking about reform of the international system...the G20 was seen as the right body for these decisions to be made at,” noted British Prime Minister Gordon Brown. U.S. President Barack Obama noted that “the G20 will take the lead in building a new approach to cooperation.” This augurs well for the G20 becoming—as Nicolas Sarkozy stated at the World Economic Forum this January, “the harbinger of global governance in the 21st century.” The G20 Council of Governors would establish strategic goals and then give the various institutions the job of carrying them out.

This G20 “Council of Governors” would focus on three main tasks:

- Setting the strategic direction of the international institutions (IMF, World Bank, WTO, and FSB) to ensure their mandates are broad enough to cover the many issues that are now falling between the cracks yet tailored enough to ensure that inefficient overlaps or mission creep are avoided;
- Pushing through the necessary changes in the voting and power structures at the IMF and World Bank to ensure that those institutions’ governance structures reflect changes in economic weight, while

at the same time infusing the WTO with direction and support from a smaller group of higher level officials; and

- Holding the international institutions accountable for implementing the directives that come from the G20 summits and giving the international institutions a forum to hold the G20 leaders accountable for their commitments to the institutions.

Providing the G20 with such a role would allow the group to set strategic direction and then use the considerable expertise and qualified personnel at each of the institutions to carry out its instructions. By giving the G20 the continuing role of coming together at least once or twice a year to perform the fiduciary duty of direction-setting and oversight for these institutions, the G20 would be assured of a consistent and on-going role in setting the course of global economic activity. Use of the G20 for this role would also give the emerging market countries a permanent and significant voice in global economic governance, getting them more engaged in addressing problems at the multilateral level and allowing them to play an important brokering role when differences between the United States and Europe threaten to cause global gridlock.

A G20 Council of Governors could also ensure that any country putting up roadblocks to the implementation of agreed-upon changes can be singled out and pressured in the “court of international opinion” to permit necessary changes to move ahead. This increased accountability would move in both directions, with the institutions themselves having access to a high-level political body to which to take concerns about failures to follow through with prior commitments. Playing this strategic leadership role would also allow the G20 to fill an oft-cited need for high-level political

engagement in the international institutions, albeit at an even higher level than initially envisaged by the reformers. Finally, inclusion of the World Trade Organization within the ambit of responsibility of this “Council of Governors” would ensure that the WTO takes its rightful place among the international institutions, in recognition of the critical link between finance, development, and

trade, and the imperative of using the expertise and rules of the WTO to ensure that private enterprise can be fully engaged in worldwide economic recovery and future prosperity. In addition to this new role for the G20, it will also be necessary to reaffirm support for the multilateral institutions at the highest political levels, and to address the explosion of regional agreements.

# 10 REAFFIRMING MULTILATERALISM IN A WORLD OF REGIONALISM

*The multilateral institutions have economies of scale, depth of expertise, greater staying power and a longer-term, broader-based approach to resolving global economic problems than any bilateral or regional agreement does.*

On the one hand, the international organizations have been taken somewhat for granted as a widely-accepted commonplace on the global scene. On the other hand, they have become the source of virulent protests and stinging political rebukes from many quarters. Those on the right, particularly in the United States, deeply resent the United Nations and see it as a sinister instrument of foreign domination. On the other side of the ideological spectrum, those on the left frequently get out the placards and line the protest routes for most meetings of the WTO or IMF and World Bank, objecting to what they see as the role of these institutions in exacerbating the worst of globalization—growing inequality that funnels wealth to the multinational corporations while leaving the poorest countries ever farther behind.

Particularly at this time of crisis, it is essential that those who understand and appreciate the critical work of these institutions stand up for them and for the broad multilateralism that they represent. Failure to do so will only undermine trust in the institutions and in the belief that global economic problems can and should be addressed globally. If nothing else, the international institutions bring both economies of scale and deep expertise that cannot be readily replaced. As the world and its problems grow more complex, this knowledge—accumulated in many countries and over a long period of time—can only be put to good use if the institutions themselves are properly maintained. The institutions also have greater staying power and a longer-term, broader-based approach to resolving global economic problems than any bilateral or regional arrangement does. They have been bringing together people and ideas from around the world for more than 60 years in countless forums, meetings, project planning sessions, and more.

Away from all the teargas and the ideological smokescreens, it is in the mundane day-to-day meetings, reports, and projects being conducted

within these institutions that multilateralism is most often advanced. Countries get in the habit of working together and come to important understandings about both the substance and the procedures for their collective action. A steady stream of information is exchanged, understandings reached, and norms established through these institutional gatherings. For example, despite the inability of the WTO to reach consensus on completion of the Doha Round, much agreement and common understanding has been achieved through the ongoing work of the various WTO committees, particularly the Council for Trade in Services and the Committee on Sanitary and Phytosanitary Measures.<sup>15</sup> While these practices don't rise to the level of formal rulemaking, they do form much of the bread-and-butter of multilateral activity that is critical if countries are going to come together in times of crisis.

The statements of G20 leaders and others supporting these multilateral institutions and their work in particular—and the principles of multilateral cooperation in general—are to be commended, and will need to be repeated over and over as the institutions continue to grapple with the often-contentious issues of the 21st century. At the same time, a number of threats to multilateralism must be acknowledged and addressed. Most importantly among these is the rapid growth of regionalism and regional alliances and trade arrangements.

<sup>15</sup> For example, the WTO Committee on Sanitary and Phytosanitary Measures has adopted a decision on the implementation of Article 4 of the SPS Agreement regarding recognition of “equivalence” of different standards, procedures to enhance transparency, and guidelines to further the implementation of the SPS provisions on regional and pest-free areas. See Andrew Lang and Joanne Scott, “The Hidden World of WTO Governance,” *The European Journal of International Law*, Vol. 20, Issue 3, 2009, pp. 575–614, citing WTO Doc S/C/M18 and WTO Doc S/CSC/M/17.



The debate over whether regional agreements—and regional trade agreements in particular—contribute to or detract from the multilateral system has grown in intensity as the number of new agreements, most recently in Asia, has skyrocketed. Indeed, in the first 45 years of the GATT—the period between 1948 and the creation of the WTO at the conclusion of the Uruguay Round—124 regional trade agreements were notified, less than three a year. By contrast, the last 15 years saw 333 new notifications of such agreements, more than 22 a year. As of October 15, 2009, 457 regional trade agreements had been notified to the WTO, 266 of which are currently in force.<sup>16</sup> The most recent is the Association of South East Asian Nations (ASEAN)-China Free Trade Area (ACFTA), launched on January 1, 2010. This is the largest free-trade area in the world by population (1.9 billion), with a combined GDP of \$6 trillion, making it the third largest (behind the European Union and NAFTA) by economic value. The ASEAN-Australia-New Zealand Free Trade Agreement (AANZFTA) also went into effect on January 1, covering 600 million people and a combined GDP of \$2.8 trillion.

Nor is trade the only area in which a spaghetti bowl of regional alliances are coming into force. The Chiang Mai Initiative Multilateralization (CMIM), a regional financial mechanism in Asia, encompassing the ASEANs, Japan, Korea, and China, set up a \$120 billion facility designed to strengthen the region's capacity to safeguard against increased risks and challenges in the global economy. The core objectives of this "Asian Monetary Fund" are (i) to address balance-of-payments and short-term liquidity difficulties in the region, and (ii) to supplement the existing international financial arrangements. As such, it represents regional competition to the IMF, albeit

with a low enough total capital base for now that the IMF will likely remain the lender of last resort even within the CMIM region.

In the development arena, the World Bank has seen an explosion in the use of trust funds, which are bilateral or regional development funds masquerading as multilateral ones. The World Bank may administer them, but the funds must be spent where and how the often sole donor designates. Over a thousand such trust funds have been established in recent years. Last year, disbursements from such trust funds equaled half of the World Bank's total disbursements. Together with bilateral development assistance, such trust funds allow donors to impose their own goals and strategy, which can bring in bilateral political pressures or a short-term or narrow focus that may not be in the best interests of a country as a whole. China, for example, has put billions of dollars into infrastructure projects in Africa while contributing only \$30 million to the International Development Association (IDA), the World Bank arm designed to help the poorest countries.

All in all, this turn to regional or bilateral arrangements in lieu of multilateral ones is huge, with approximately 50 percent of all trade occurring under such agreements and about 65 percent of all aid currently coming from trust funds, bilateral aid funds, or "vertical" loans or grants focused on a particular issue. Why such a dramatic shift? Many countries around the world have turned away from multilateralism and the multilateral institutions for a number of reasons. First, there are non-institutional alternatives to the multilateral system—ranging from a broad array of private investment tools that supplant the IMF to huge infrastructure projects that are financed by foreign governments or other aid funds, often undermining the role of the World Bank. Second, many developing countries are skeptical about institutions set up by the transatlantic powers in

*This turn to regional or bilateral arrangements in lieu of multilateral ones is huge, with approximately 50 percent of all trade occurring under such agreements and about 65 percent of all aid currently coming from trust funds, bilateral aid funds, or "vertical" loans or grants focused on a particular issue.*

<sup>16</sup> World Trade Organization, "Report of the Committee on Regional Trade Agreements", WT/Reg/20, 16 Oct. 2009.



*The multilateral institutions need to recognize that the regional agreements are massive in magnitude and add enormous complexity to the system, but they are here to stay and need to be accommodated and incorporated into the multilateral system.*

which they don't have a significant voice or any great confidence that the institutions will address their needs. Third, they have found regional agreements easier to reach, either because they don't require solving some of the hardest problems on the table in multilateral negotiations—for example, agricultural subsidy issues at the WTO—or simply because reaching an agreement on a bilateral or regional basis is easier than trying to reach an agreement among the multitude of parties to any agreement at the multilateral level.

The downsides of this rush to regionalism are many. The time, energy, and resources required to negotiate bilateral or regional agreements are considerable, and by necessity take away valuable time, resources, and political capital available to countries to devote to multilateral agreements. At the same time, bilateral or regional agreements are much more subject to the vagaries of domestic politics—indeed, they are often initiated in response to particularistic commercial or foreign policy pressures. Then, once they are in force, most of these agreements have weak or non-existent dispute settlement mechanisms, making commitments under such agreements harder to enforce. Bilateral and regional agreements often have unique rules and provisions, which increases overall transaction costs in the system and makes it difficult for developing countries to understand what they need to do to comply with a wide array of differing sets of rules. On the trade side, such agreements often exclude

particular products or don't allow for cumulation of inputs or resources from countries outside of the particular agreement, which can lead to inefficiencies and to hub-and-spoke systems of trade in which power-based arrangements begin to erode the protection of a rules-based non-discriminatory multilateral trading system.<sup>17</sup> Finally—and most importantly—proliferating preferential agreements by their very existence send a strong signal of a growing lack of faith in multilateral institutions and the multilateral system.

As such, it is imperative that the multilateral system work to fix problems that act as a deterrent to deeper engagement by developing countries while at the same time working to bring the various bilateral and regional arrangements within their systems. The multilateral institutions need to recognize that the regional agreements are massive in magnitude and scope and have added enormous complexity to the system, but that at the same time they are here to stay. Most urgently needed from the multilateral institutions are clear guidelines for any such agreements to ensure that they are stepping stones to multilateralism rather than barriers to entry for anyone outside any given regional or bilateral arrangement.

---

<sup>17</sup> The potential for regional trade agreements to undermine the multilateral system have been widely discussed. See for example Jagdish Bhagwati, *Termites in the Trading System: How Preferential Agreements Undermine Free Trade*, Council on Foreign Relations (2008).

# 11 TRANSATLANTIC MULTILATERALISM FOR THE 21ST CENTURY

During the critical period of the Bretton Woods conference of 1944 and in the months that followed, a large part of the world picked itself up from the ruins of depression and war and rallied around the vision—largely set forth by the United States and Great Britain—to create institutions and accords that would prevent a repetition of the disasters of the 1930s by allowing for global economic cooperation and multilateral governance. Then-U.S. President Franklin Delano Roosevelt, in his last address to the U.S. Congress, declared that “the world will either move toward unity and widely shared prosperity, or it will move apart,” noting that the then-emerging plans for the Bretton Woods institutions and the global trading system represented the chance “to lay the economic basis for the secure and peaceful world we all desire.”

The present global economic crisis has not been of the same order of magnitude of the events of the 1930s. But it does represent another transformative moment in world history. In particular, it presents the United States and Europe with another opportunity to exercise shared transatlantic leadership to ensure that the vision of their past leaders can be preserved, updated, and carried forward into the 21st century with all the challenges it brings. What do Europe and the United States need to do to meet this challenge?

First, they need to commit to not give up on the multilateral economic institutions, but to reform them instead. Together, the United States and Europe created these multilateral institutions and they have as much to gain as ever in keeping them at the core of the global economic architecture. However, ensuring that these institutions remain relevant, legitimate, and effective will mean some significant changes in the manner in which both the United States and Europe participate in their operations. These changes are an opportunity to show real leadership on the world stage at the cost of some concessions in the formal power structure.

Agreeing to make these concessions would also send a powerful signal to the rest of the world that they can have faith that these institutions are changing to accommodate shifting relationships in the global economy and an equally powerful affirmation by the transatlantic powers of their continuing reliance on multilateral institutions.

For its part, the United States should give up on both the unwritten rule that the head of the World Bank must be an American and the insistence that it retain veto power over matters requiring a supermajority. In addition, the United States should support the use of the G20 as a strategic steering group or “Council of Governors” for the World Bank, IMF, and WTO to ensure a strong G20 role in strategy formulation and coordination that would also give greater voice to the emerging market economies.

In the same vein, the member states of the European Union should give up on the unwritten rule that the head of the IMF must be a European, and work to consolidate European votes and seats at the IMF and World Bank either into a single European seat (which would give Europe the single largest voting share) or at least consolidate its seven partial seats with the bigger European economies so that Europe ends up with no more than four seats. As with the United States, the European Union and its member states should also lend their support to the G20 as the “steering committee of the global economy.”

For Europe, the form of European participation in the Bretton Woods institutions presents a challenge and an opportunity to resolve the best way to ensure the strongest collective European voice in global economic governance. The coming into force of the Lisbon Treaty gives the European Union a formal international legal personality, and all around the world the EU is reorganizing its representation, a process that will continue with the

*In order to save the institutions they started, the U.S. and Europe need to give up some of their formal power in order to allow more legitimate and more relevant institutions to emerge.*

*Today, at the WTO, Europe speaks with one voice, through sole representation by the European Commission. The opposite is the case at the Bretton Woods institutions.*

formation of the External Action Service. A reform of the governance structure of the international economic institutions would give Europe another opportunity to put this new status into operation.

Today, at the WTO, Europe speaks with one voice, through sole representation by the European Commission. The opposite is the case at the Bretton Woods institutions, where the European Union has no formal place and can only act through the voice of certain member states. Nor does the Eurozone have a formal place at the IMF. At the G20, the European Union and the European Commission have been present—but so, too, have been individual member states (France, Germany, Italy, and the United Kingdom, later joined by Spain and the Netherlands), with some of these member states overshadowing the European Union. Reforming the manner of European participation in the Bretton Woods institutions could be a win-win for Europe. It would allow Europe to show leadership and a commitment to the modernization of the multilateral institutions while at the same time consolidating European power in a single but larger voting share. But it will not be easy. The three member states with permanent seats—France, Germany, and the United Kingdom—will no doubt resist giving up their exclusive rights. Many of the issues related to financial regulation and reform are still carried out at the national level, even within Europe and within the Eurozone. However, the opportunity to obtain more influence by acting collectively in this one arena of international economic institutional governance ought to be compelling for Europe. These institutions do not raise the same political problems of European consolidation that would be present at the UN or in other fora. Participating as one Europe could be seen as furtherance of the process of a coordinated European approach that was begun in preparation for the G20 Leaders Summits and of the Lisbon Treaty's goal of making the European voice in the world stronger.

Nonetheless, on paper, all of this could be seen as a dramatic loss of power on both sides of the Atlantic. But as a practical matter, a diminution in sway over the institutions of global economic governance could result in longer-term gains that would stem from stronger, more legitimate, and more effective institutions that operate to the continuing benefit of the United States and Europe and the kind of stable, open, rules-based global economy they both support. If the process and criteria for selecting the heads of the IMF and World Bank were solely merit-based, and if the United States and European Union nominated highly-qualified candidates, they would likely continue to take their turn in having their nationals serve in leadership roles. Moreover, while the exact voting share of countries is an important symbol of their power, few if any formal votes are taken in practice. In the process of finding sufficient support for any given proposal short of a formal vote, the consolidation of Europe into a single voice may result in more, not less, influence. Moreover, some diminution in the voting share of the United States or Europe would still leave both powers with the ability to block objectionable changes simply by finding a small handful of other countries to join them.

At the WTO, the concerns over and need for transatlantic leadership are somewhat different, while the challenges of effectiveness, legitimacy, and relevance are the same. Unlike the IMF and the World Bank, the WTO does not have an executive board or a management board, nor does the WTO Secretariat have the power to set priorities or propose new rules or formal structures to approve new rules other than through consensus—and traditionally only through rounds of negotiations. This means that the WTO does not need to engage in any formal rebalancing—certainly not in the direction of a further devolution or redistribution of power. However, the WTO membership does need to form new alliances and groups that would create the basis for decision-making in the absence of complete consensus. It is in putting together

these alliances that the United States and the European Union should play a leadership role by taking seriously the recommendations of the Sutherland Report, the Warwick Commission, and other contributions to put in place alternatives to the single undertaking—an “all-for-one and one-for-all” consensus only process. U.S. and European leaders should ensure that a serious debate about the WTO’s governance structure and its place in the global economic architecture takes place now, while leaders from around the world are focused on all three pillars of the system and should make it clear that this examination can be conducted without detriment to the ongoing attempts to conclude the Doha Round negotiations—and in fact could even contribute to their successful conclusion. This is the moment for the WTO to take its rightful place as an equal partner with the IMF and the World Bank in the global economic system.

Second, the United States and Europe should use the G20 as the most efficient mechanism to insert high-level involvement in the governance of these institutions, particularly their strategic direction setting and the coherence among them. They need to ensure that the mandates of these institutions are modernized to cover the many issues that are currently going unaddressed—including food security, energy policy, climate change, competition policy, and corruption—while protecting against duplication among them. They also must take seriously the commitment to allow their own macroeconomic policies to be subject to real scrutiny by the G20 and the IMF for consistency with the G20 Framework for Strong, Sustainable, and Balanced Growth. Moreover, both the United States and the EU need to take seriously the proposals for reform of these institutions and to stick with the reform process until the necessary renovations of the institutions are completed.

Third, the United States and the European Union should reaffirm their commitment to multilateralism by working to multilateralize the

tangle of their own regional agreements and to adopt a set of guidelines for any further agreements that ensure that they do not detract from or undermine the multilateral system.<sup>18</sup> As in many other areas, the European Union and the United States have been at the forefront of regionalism. The European Union itself is a regional agreement—the largest economic free trade area in the world, followed by the North American Free Trade Agreement, linking the United States, Canada, and Mexico. Given their leadership roles in both multilateral and regional growth, the United States and Europe should also lead the way in finding a way to multilateralize these agreements, particularly the agreements they each have in common with other countries, in a manner which brings them closer to multilateralism. Currently, the United States and the EU remain each other’s largest trading partners—far exceeding their trade with any other country. For example, U.S. two-way trade in goods with the EU totaled \$988 billion in 2009, while its two-way trade with China was \$366 billion. However, high on the list of significant trading partners for both the US and the EU are a number of countries with whom both have negotiated a free trade agreement, most notably Canada (the United States’ second largest partner and Europe’s fifth), South Korea (the sixth largest trading partner for both the United States and the EU) and Mexico (the fourth largest partner for the United States and tenth for the EU). If these common agreements alone could be reshaped into multilateral agreements, the United States and the EU will have done much to bring a substantial amount of trade back into the multilateral fold.

<sup>18</sup> The concept of “multilateralizing” regional agreements has been much discussed in academic and other forums, including at the September 10-12 2007, conference at the WTO, “Multilateralizing Regionalism: Challenges for the Global Trading System.” See in particular, Richard Baldwin’s “Multilateralising Regionalism: Spaghetti Bowl as Building Blocks on the Path to Global Free Trade,” *The World Economy* 29 (2006).

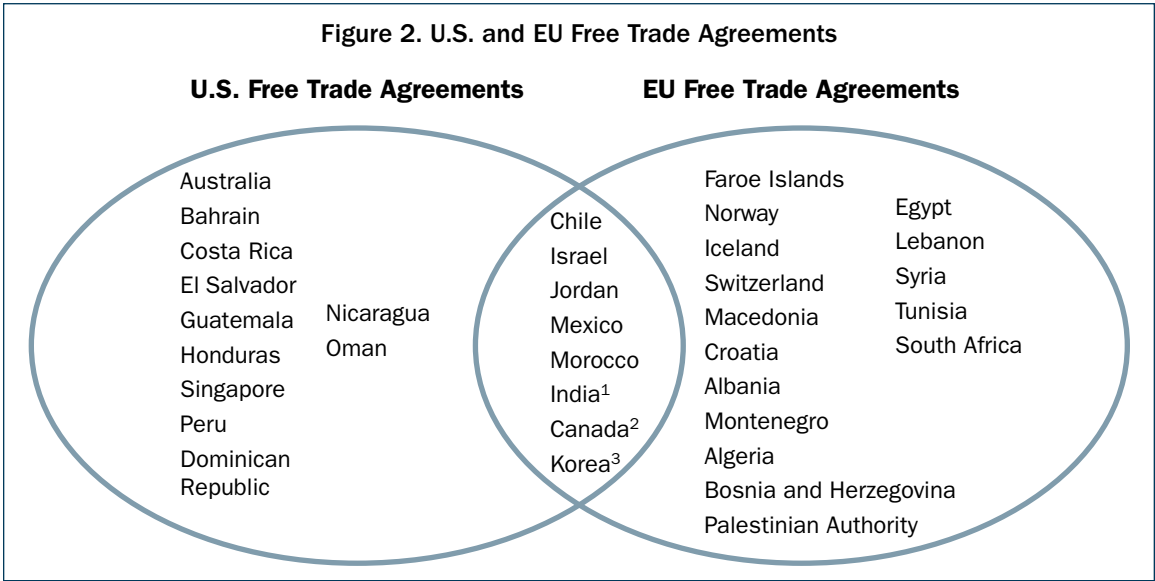
The most important contribution to be made is to agree upon principles to guide such efforts as a way of distinguishing those agreements that are acceptable within a multilateral system and those that are not. “Acceptable” agreements would include those that:

- Do not create conflicts with members’ obligations under multilateral agreements, such as the WTO Agreement or the IMF’s Articles of Agreement.
- Are at least as transparent as multilateral agreements.
- Require full disclosure of all the details to the multilateral institutions and subject the regional agreement to potential assessment by the relevant multilateral institution for

significant inconsistencies with multilateral obligations.

With respect to trade agreements, much work has already been done in many forums on the specifics of harmonizing rules of origin, or providing opportunities to cumulate inputs into the manufacture of goods, resolving conflicts between dispute settlement provisions, mutually recognizing regulatory approvals and more.<sup>19</sup> The European Union and the United States need to agree to undertake this work now in order to show others that their own regional agreements can put them on the path to greater multilateral integration.

<sup>19</sup> See Richard Baldwin and Patrick Low, *Multilateralizing Regionalism*. Antoni Esteveadeordal and Kati Suominen “Bridging Regional Trade Agreements in the Americas,” Special Report on Integration and Trade, Inter-American Development Bank.



Source: USTR

The United States has signed free trade agreements (FTAs) with Colombia, Korea, and Panama, but Congress must enact legislation to approve and implement each agreement in order for them to go into effect.

Source: EU Trade-European Commission (Jan. 11, 2010)

<sup>1</sup>Both the United States and the EU are in the process of negotiating an agreement with India.

<sup>2</sup>The United States and Canada have an FTA in effect. The EC and Canada negotiated a common working document in Dec. 2009; final confirmation of an FTA is pending further consultation.

<sup>3</sup>While the U.S. has already signed a free trade agreement with Korea, Congress has yet to enact legislation to approve it. The EC's FTA with Korea was initialed in Oct. 2009. The text of the FTA must be translated into all EU languages before the ratification process can proceed.

# 12 CONCLUSION

The way forward—for the international community as a whole, and for the transatlantic partners in particular—is now clear. To cope with the increasing complexity of world affairs, in which the challenges themselves are growing more difficult and reaching agreement among the large number of players is ever more like a huge multidimensional chess game, the institutions of global economic governance are in urgent need of renovation. The status quo is not an option—let alone the status quo ante, before the economic crisis struck. Failure to modernize the international economic institutions in all likelihood will mean watching them atrophy and decay. The end result would be even greater fragmentation of global economic governance into a patchwork of overlapping, competing, and conflicting regional and bilateral arrangements that would reduce the ability of both individual countries and the international community as a whole to act and to find solutions to the most urgent problems of the day.

This need not be the case. In spite of Copenhagen, in spite of the eight years of crisis and stalemate in the Doha Round negotiations, in spite of proliferating regionalism, it is still possible to save

multilateralism and to preserve the architecture that has served the international community well. Reforms can be made to our existing institutions that both preserve the strong role and voice of the United States and European Union while simultaneously encouraging stronger participation and commitment from the emerging market countries. By acting responsibly and showing leadership in the redistribution of power, giving emerging market countries more say over the strategic direction of the existing global economic institutions, the United States and Europe can lead the way in preserving and extending the benefits of the multilateral economic order they created. By working with the emerging market countries through the mechanism of the G20 Leaders Summit, they can provide a “Council of Governors” for the global economic institutions. In this manner, the United States and the European Union can continue to provide the kind of stewardship and direction of the global economy they showed in the second half of the 20th century and that is so sorely needed amid the increasing complexities and growing challenges of the 21st.



# 13 BIBLIOGRAPHY

- Bhagwati, Jagdish. *Termites in the Trading System: How Preferential Agreements Undermine Free Trade*. New York: Council on Foreign Relations, 2008.
- Baldwin, Richard and Patrick Low. *Multilateralizing Regionalism: Challenges for the Global Trading System*. New York: Cambridge University Press, World Trade Organization, 2009.
- Baldwin, Richard E. "Multilateralizing Regionalism: Spaghetti Bowls as Building Blocks on the Path to Global Free Trade." *The World Economy*, 29, 2006.
- Bergsten, C. Fred. Keynote Address. "A Blueprint for Global Leadership in the Twenty-First Century." Peterson Institute for International Economics, Global Human Resources Forum. Seoul, Korea. November 4, 2009.
- Blustein, Paul. *Misadventures of the Most Favored Nations*. New York: Public Affairs, 2009.
- Blustein, Paul. *The Chastening: Inside the Crisis that Rocked the Global Financial System and Humbled the IMF*. New York: Public Affairs, 2001.
- Coffey, Peter and Robert J. Riley. *Reform of the International Institutions: The IMF, World Bank and WTO*. Northampton: Edward Elgar Publishing, 2006.
- Cooper, Richard N. and Edwin N. Truman. "The IMF Quota Formula: Linchpin of Fund Reform." Policy Brief 07-1. Washington: Peterson Institute for International Economics Policy, 2007.
- De Rato, Rodrigo. "Is the IMF's Mandate Still Relevant?" *Global Agenda*. January 2005.
- Eichengreen, Barry. "The G20 and the Crisis." *Responses to the Global Crisis: charting a progressive Path*. Progressive Governance Conference handbook, March 2009. <http://www.econ.berkeley.edu/~eichengr/reviews.html>.
- Eichengreen, Barry. "Five Ideas for Strengthening the IMF," March 2009. [http://www.econ.berkeley.edu/~eichengr/responses\\_global\\_five\\_ideas.pdf](http://www.econ.berkeley.edu/~eichengr/responses_global_five_ideas.pdf).
- Einhorn, Jessica. "Reforming the World Bank." *Foreign Affairs* Vol. 85, 1 (January/February 2006).
- Estevadeordal, Antoni and Kati Suominen. *Bridging Regional Trade Agreements in the Americas*. Washington: Inter-American Development Bank, 2009.
- Freeman, Richard B. *America Works: Critical Thoughts on the Exceptional U.S. Labor Market*. New York: Russell Sage Foundation, 2007.
- Gilbert, Christopher L. and David Vines. *The World Bank: Structure and Policies*. New Haven: Cambridge University Press, 2000.
- "Governance of the IMF: An Evaluation." Independent Evaluation Office, International Monetary Fund.
- Gresser, Edward. "Geo-Politics." *Democracy Journal*, Fall 2009.
- Haass, Richard N. "The Case for Messy Multilateralism." *Financial Times*. January 5, 2010.
- Head, John W. *Losing the Global Development War*. Boston: Martinus Nijhoff Publishers, 2008.
- Henning, Randall C. "Regional Arrangements and the IMF." Conference on Reform of the IMF. Institute for International Economics, September 23, 2005.
- Horn, Henrick, Pero C. Mavroidis and Andre Sapir. "Beyond the WTO? An Anatomy of EU and US Preferential Trade Agreements." Bruegel Blueprint Series; 7 (2009). [http://www.bruegel.org/uploads/tx\\_btbbreugel/bp\\_trade\\_jan09.pdf](http://www.bruegel.org/uploads/tx_btbbreugel/bp_trade_jan09.pdf).

Hubbard, R. Gleen and William Duggan. *The Aid Trap*. Columbia Business School. New York: Columbia University Press, 2009.

Hufbauer, Gary and Kati Suominen. *Globalization at Risk: Challenges to Finance and Trade*. New Haven: Yale University Press, 2010.

“IMF Governance—Summary of Issues and Reform Options.” Strategy, Policy, and Review Department and the Legal Department, July 2009.

Johnson, Simon, Peterson Institute for International Economics. Testimony before the Subcommittee on Terrorism, Nonproliferation and Trade, Committee on Foreign Affairs. “US Foreign Economic Policy in the Global Crisis.” U.S. House of Representatives, March 12, 2009.

Lamdany, Ruben and Leonardo Martinez-Diaz. *Studies of IMF Governance: A Compendium*. The Independent Evaluation Office of the International Monetary Fund, 2009.

Lang, Andrew and Joanne Scott. “The Hidden World of WTO Governance.” *The European Journal of International Law*, Vol. 20, Issue 3, 2009, pp. 575-614.

Lombardi, Domenico. “Report on the Civil Society (Fourth Pillar) Consultations with the International Monetary Fund on Reform of IMF Governance.” New Rules for Global Finance Coalition.

Mattoo, Aaditya and Arvind Subramaniam. “From Doha to the Next Bretton Woods: A New Multilateral Trade Agenda.” *Foreign Affairs* Vol. 88, January/February 2009.

Manuel, Trevor. *Committee on IMF Governance Reform Final Report*. Committee on IMF Governance Reform, March 24, 2009. <http://www.imf.org/external/np/omd/2009/govref/032409.pdf>.

Martinez-Diaz, Leonardo. “Toward A Grand Bargain on World Bank Reform.” Washington: Brookings Institution, December 16, 2009. [http://www.brookings.edu/articles/2009/1216\\_world\\_bank\\_martinez\\_diaz.aspx](http://www.brookings.edu/articles/2009/1216_world_bank_martinez_diaz.aspx).

Moyo, Dambisa and Nial Ferguson. *Dead Aid: Why Aid is not Working and How there is a Better Way for Africa*. New York: Farrar, Straus and Giroux, 2009.

Nelson, Rebecca. “The G20 and International Economic Cooperation: Background and Implications for Congress.” Congressional Research Service 7-5700, December 9, 2009.

Paloni, Alberto and Maurizio Zanardi. *The IMF, World Bank and Policy Reform*. New York: Routledge, 2006.

Patrick, Stewart. “Prix Fixe and à la Carte: Avoiding False Multilateral Choices.” *The Washington Quarterly*, October 2009.

*Repowering the World Bank for the 21st Century: the “Zedillo Commission Report.”* High-Level Commission on Modernization of World Bank Group Governance, October 2009.

“Status of Projects in Execution – FY09 SOPE,” Operations Policy and Country Services, World Bank, October, 2009

Steger, Debra P. *Redesigning the World Trade Organization for the Twenty-first Century*. Centre for International Governance and Innovation (CIGI) and Wilfrid Laurier University Press, 2010.

Truman, Edwin M. *Reforming the IMF for the 21st Century*. Special Report No. 19. Institute for International Economics, April 19, 2006.



*The Future of the WTO: Addressing institutional challenges in the new millennium.* The Sutherland Report. Consultative Board to the Director-General Supachai Panitchpakdi. World Trade Organization, 2004.

“The World Bank Annual Report 2009.” The World Bank, 2009.

Vines, David and Christopher L. Gilbert. *The IMF and its Critics*. New Haven: Cambridge University Press, 2004.

## G|M|F OFFICES

WASHINGTON • BERLIN • BRATISLAVA • PARIS  
BRUSSELS • BELGRADE • ANKARA • BUCHAREST

[www.gmfus.org](http://www.gmfus.org)

