FOCUS ON WHAT ASIA WANTS

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Framing the Issue

Five Asian countries will participate in the G-20 London Summit: China, India, Indonesia, Japan, and South Korea. As a group, they represent 44 percent of the world's population. In GDP terms, however, they represent only 18 percent of global GDP, with Japan leading and Indonesia trailing the group.

The London Summit is all about the global economic and financial crisis. Because the United States has the world's biggest economy, and because the crisis originated there, the American voice at the London Summit will without question be the dominant one. Two factors reinforce this special status: the unrivaled military power of the United States and the phenomenal global popularity of its new president, Barack Obama.

Added together, these factors put the United States in an impossible position. The constraints on U.S. action are as great as the expectations. President Obama's policymaking team is far from being fully staffed and cannot have engaged in the consultations with its global partners to the extent demanded by the circumstances. The risks posed by the London Summit for the United States and the world may be much greater than people are generally assuming.

While the United States is not a "region" per se, it is big enough to be considered as one in this context. After the United States, Europe views itself as the most important region represented at the Summit, but a case can be made that Asia deserves the number two ranking. The case begins with its population weight, close to half of the world's population. Although we live in an increasingly democratic one-person-one-vote world, policy lags seriously behind this reality. The more fundamental reason for giving priority to Asia over Europe at this moment is Asia's position as the major source of the high savings and the large balance of payments surpluses that mirror the low savings and balance of payments deficit of the United States. A strategy that is not seen as leading to the correction of this imbalance will not be credible.

The Asian region, however, has two handicaps relative to Europe: history and culture. Events in the past hundred years have left scars within the region, especially between Japan and the rest and between China and India. Deeper cultural differences divide the region along religious and ethnic and development lines. Such differences also exist in Europe but are muted. Nowhere in Europe do they approach the difference within the smaller 10-nation ASEAN community between wealthy, over-governed Singapore and impoverished, miserably-managed Myanmar.

Policy Considerations

The headline issue in the run-up to the London Summit has been the tug of war between the United States seeking to give priority to global fiscal stimulus and Europe seeking to give priority to regulation of financial institutions and markets. None of the Asian countries seem to have strong views on the regulation part of the agenda, presumably reflecting their relatively repressed financial systems. On the fiscal stimulus issue, China's position is critical, and it is isolated. Although it has announced the largest stimulus package in dollar terms among the five Asian participants, China came into the crisis from a position of fiscal surplus and appears to have room to do considerably more. The other four Asian participants would like to see China do more to stimulate domestic demand because of the direct and positive impact on their own economies.

A core Chinese concern in the run-up to the London Summit was revealed on March 13 when Prime Minister Wen Jiabao said he was "worried" about the U.S. Government's huge indebtedness to China. This concern is not exclusive to China. Japan has a comparable exposure and the other three Asian participants also have substantial foreign exchange reserves that are heavily invested in U.S. Treasury securities. The Asian participants are united in placing the blame for the crisis squarely on the United States and expecting the United States to do the most to overcome it. Asia's concern is by no means new. The lead headline in the *Financial Times* on November 23, 2004, was "China tells U.S. to put its house in order."

A third issue, however, looks like the critical one for the five Asian countries going to the London Summit: the future role of the International Monetary Fund (IMF). On economic grounds, the case for increasing the resources of the IMF is compelling, but the politics of such an increase are daunting for Asia on three levels. First, the financial crises in Thailand, Indonesia, and Korea in 1997 left Asian countries feeling mistreated by the IMF. They have been saying since then that they must maintain large foreign exchange reserves because they cannot be certain of getting timely, sufficient, and fairly-conditioned help from the IMF the next time a crisis erupts. Second, it is difficult for Asian countries (except for Japan) to make the case domestically for contributing more resources without a substantial increase in their voting shares, which are now too small but almost all measures. Third, China's voting share is now the sixth largest while Japan is in second place after the United States. It will be hard for China to be "invested" in the IMF as long as its voting share is smaller than Japan's, but Japan does not appear ready to accept sharing second place with China (France and the United Kingdom are tied for fourth place).

A decision to increase the IMF's resources is greatly complicated by the existence of four distinct routes. The route in normal times is a general quota increase that raises the quotas of all members in the same proportion. A doubling of quotas, which can be justified easily on economic grounds, would raise total quotas from $320 billion to $640 billion. The route already in place for times of stress involves activating two lines of credit: the General Arrangements to Borrow (GAB) and the New Arrangements to Borrow (NAB). The United States favors this route, by adding $500 billion to the existing arrangements, which together now total $50 billion. A third route used in the past has been bilateral loans to the IMF. Japan has already committed $100 billion in this form, which could be matched easily by China and other countries with ample foreign exchange reserves such as oil producers like Saudi Arabia. The easiest route could be for the IMF to issue its own currency—Special Drawing Rights (SDRs)—to all members in proportion to their quotas. The IMF issued SDRs twice in the 1970s, but not again since then. Ted Truman, a highly regarded former U.S. Treasury official, has floated a proposal for a third issue now on the order of $250 billion. None of these routes are mutually exclusive; any combination is possible.

Action Items for Global Coordination

It will be devilishly difficult to reach agreement at the London Summit on a package that will increase the resources of the IMF quickly because of the voting share issue and other governance issues such as the process for selecting the Fund's Managing Director. Moreover, a deal without the full support of Japan, China, and India will probably not provide the fillip to confidence that the London Summit must deliver to put the world firmly on the road to recovery.

Perhaps the biggest question is whether the rest of the world is prepared to accept a Made-in-the-USA deal, even if delivered on a silver platter by President Obama. Politically, the most palatable deal could be one that has a Made-in-Asia label. What better proof that the U.S. is ready to stop preaching and work in partnership with others to build a more sustainable and harmonious world?