



# THE TOP 10 GLOBAL ECONOMIC CHALLENGES FACING AMERICA'S 44TH PRESIDENT

By Lael Brainard

## THE 2008/2009 TOP 10 GLOBAL ECONOMIC CHALLENGES

Edited by Lael Brainard

1. RESTORING FINANCIAL STABILITY  
By Eswar Prasad
2. SETTING THE RIGHT GREEN AGENDA  
By Warwick McKibbin, Adele Morris and Peter Wilcoxon
3. EXERCISING SMART POWER  
By Lael Brainard and Noam Unger
4. REIMAGINING GLOBAL TRADE  
By Paul Blustein
5. NAVIGATING CHINA'S RISE  
By Wing Thyee Woo
6. DECIPHERING "RUSSIA, INC."  
By Clifford Gaddy
7. ENGAGING AN EMERGING INDIA  
By Eswar Prasad
8. REVITALIZING TIES TO LATIN AMERICA  
By Mauricio Cárdenas and Leonardo Martínez-Díaz
9. SUPPORTING AFRICA'S GROWTH TURNAROUND  
By John Page
10. PURSUING A POSITIVE AGENDA FOR THE MIDDLE EAST  
By Navtej Dhillon, Djavad Salehi-Isfahani and Tarik Yousef

With America's next president taking office at a moment of consequential global challenges that even the most powerful nations cannot resolve on their own, there is a clear need for leadership. But with U.S. financial turmoil reverberating against the backdrop of a profound global shift in economic power, America's capacity and will to provide that leadership are less clear. Nonetheless, given America's enormous stakes in a strong and resilient global economy, it will be critical for America to lead on the main challenges we face today.

## THE GLOBAL CONTEXT

The "made in the USA" financial crisis comes at the same time economic policymakers are confronting the emergence of a group of rising powers, from China and India to the Gulf states and Russia. We are now living in a rapidly shifting economic environment. Following 35 years of strong economic output by the Group of Seven economies, during which they commanded approximately 65 percent of the global output and the so-called "BRIC"—Brazil, Russia, India, China—economies accounted for about 7 percent, we have seen the Group of Seven's share falling to 58 percent over the past five years and the BRIC's share rising to more than 11 percent. By 2030, according to Brookings expert Homi Kharas, the two groups are expected to converge towards parity, with each accounting for about one-third of world output. The BRICs and other emerging economies are booming, integrating into the global economy, and learning to assert their interests more forcefully.

This revolution in national income shares is emblematic of a broader global dispersion of wealth and economic dynamism. In contrast to the shift of the world's financial epicenter from the City of London to Wall Street in the interwar period, stock

# INTRODUCTION: THE TOP 10 GLOBAL ECONOMIC CHALLENGES FACING AMERICA'S 44<sup>TH</sup> PRESIDENT

markets and commodity exchanges are now proliferating in multiple financial centers; thus, in 2006, 18 of the 20 largest initial public offerings took place outside the U.S. and were spread out among 11 stock exchanges. Indian and Brazilian multinationals have made major acquisitions of flagship European and North American brands. And in 2007, a new breed of sovereign wealth funds injected more capital into shaky U.S. and European financial institutions than the International Monetary Fund provided to Asian economies at the height of their financial instability in 1997.

## THE CHALLENGE

The rapid growth of the rising powers is creating enormous opportunities but also putting considerable strain on resources from food to water to energy, contributing to global inflationary pressures, just as humanity is waking up to the urgent need to wean the world's economy from its centuries-long dependence on carbon. Growing global integration also creates growing interdependence and mutual vulnerability—most visibly to financial turmoil—but also to food and energy shortages, pandemics, and vortexes of conflict and poverty.

The size, complexity, and opacity of financial transactions in the context of an outdated regulatory structure have shredded the traditional U.S. financial policy playbook. The recent actions by the U.S. Treasury and the Federal Reserve to intervene in the U.S. financial system through unconventional means on an unprecedented scale have added to foreign skepticism over Washington's conventional liberalization agenda. It will be many years before U.S. policymakers will be able to make the case for the full liberalization of capital flows in emerging markets. To many audiences in emerging markets, China's heterodox growth model, in particular, has gained considerably greater allure.

Growing integration on the real side of the global economy is similarly complex. Though trade ministers sign all types of bilateral and mini-lateral trade agreements, and global trade flows are going gangbusters, multilateral and major regional trade negotiations are going bust.

Although polarization has grown on trade, there is growing convergence on the critical importance of global development. While the U.S. public has rallied around

grassroots efforts to raise spending on HIV/AIDS and provide debt relief, U.S. military and foreign policy circles have come to recognize the fight against global poverty as a fight of necessity—not only because personal morality demands it but also because U.S. national security does as well. These two converging strands have helped provide the biggest boost to U.S. foreign assistance in decades, along with a proliferation of uncoordinated institutional arrangements to administer it.

In the next few years, every one of these challenges will be further complicated by the belated and patchwork attempts to mitigate and adapt to a changing global climate. A fundamental transformation of the world's economic paradigm away from the carbon foundations of the past nearly two centuries will require vast global flows of technology and capital.

## AMERICA'S OPPORTUNITY

The top 10 global economic challenges awaiting the next President defy easy solutions but are vital to the prosperity and stability of America and the world:

- 1. Restoring financial stability:** With our financial troubles at the center of the current global vortex, the U.S. has important obligations to strengthen the global financial system, including by strengthening our own financial regulation and diminishing our reliance on foreign credit. The next U.S. president should work with the international community to develop a common agenda for managing capital flows, including increasing flexibility in exchange rates to facilitate the adjustment of persistent imbalances, developing global codes for improved transparency of new players such as sovereign wealth funds, and updating the mission and governance of the international financial institutions to address today's challenges and engage today's players.
- 2. Setting the right green agenda:** It is past time to muster the political will to act on climate change at the national level while also working to forge international agreement so that markets and regulatory policy will provide a consistent set of incentives to wean the economy from carbon foundations. It will require a delicate balance of persuasion and pressure to induce the fastest growing

emitters of greenhouse gases to take action in the face of concerns about growth. It will require much assistance and financing to help the most vulnerable nations adapt. And it will inevitably risk trade frictions as competitiveness concerns come to the fore if America takes on obligations ahead of its trade partners.

3. **Exercising smart power:** Investing in the education, health, livelihoods, and the security of the world's poorest not only makes Americans feel good about themselves but also makes the world feel good about America. It is critical to capitalize on the upsurge of support for global development among the U.S. public evidenced in increased advocacy, service, and individual giving to make sustained investments in lifting up the lives of the poor. It is critical to increase not only resources but also the impact of each dollar spent.
4. **Reimagining global trade:** Americans feel most secure about global engagement when they are well equipped to compete and have insurance against economic risks. This requires vigorously enforcing the trade rules and investing in economic competitiveness—lifelong learning, innovation, infrastructure—to widen the circle of winners, while at the same time developing effective and portable insurance systems for unemployment, health, pension, and earnings to provide economic security in the face of job dislocation.
5. **Navigating China's rise:** America will need to engage intensively bilaterally, regionally and multilaterally to shape China's continued integration with the international system of rules. On issues such as climate change, enforcement of trade rules and exchange rate adjustment, where the stakes are simply too high to ignore, America should look for cooperative mechanisms to advance its goals where possible but continue to press bilaterally and better deploy regional and international mechanisms where necessary.
6. **Deciphering "Russia, Inc.":** Difficult as it may be to accomplish, America nonetheless has significant interests in alternately coaxing and goading a resurgent, resource nationalist Russia toward international norms and cooperation on energy, trade, financial integration and security more broadly.
7. **Engaging an emerging India:** America has enormous interests in India's successful integration into the global economy as the world's most populous democracy engages in the task of lifting hundreds of millions out of poverty. Yet India poses challenges in areas ranging from integrating global agricultural markets to combating climate change, and the country's success in global high value services markets has complicated America's internal debate on trade. America must look for areas of cooperation where possible and deepen bilateral engagement broadly in order to make progress on its agenda.
8. **Revitalizing ties to Latin America:** The United States has deep and abiding interests in vibrant economic relations with the nations of the Western hemisphere and a growing population with roots in the region—which are not matched by the quality of its engagement. America must become a stronger partner to its neighbors and engage on issues of mutual concern, including on energy, environmental protection, economic competitiveness and social policies.
9. **Supporting Africa's growth turnaround:** Many African nations have experienced dramatic, sustained growth during the past decade due in part to improved policy frameworks and increasing global demand for their products. America can become a stronger and steadier partner to Africa as it navigates economic challenges by supporting global standards for natural resource management, opening markets to African products, supporting vibrant private enterprises, supporting African efforts to enhance regional security and build resilience to climate change, and both increasing and improving the quality of development assistance.
10. **Pursuing a positive agenda for the Middle East:** Though America's leaders view the Middle East through the prism of Islamic radicalism, many of the region's leaders see their own core challenge as providing educational and economic opportunities for their burgeoning youth populations. America can build partnerships in the region based on trust and mutual respect if it aligns its agenda on economic and political reform with the aspirations of the majority of the region's people: the young who are striving for opportunity and global integration.