13

A New Steering Committee for the World Economy?

C. FRED BERGSTEN

My colleague Ted Truman, who superbly organized this conference, begins his overview chapter by noting correctly that "[t]he world needs a strong and effective International Monetary Fund. . . ." Unfortunately, the IMF has instead become weak and ineffective.

The Basic Problem

The Fund's management and staff have courageously publicized the current global imbalances that increasingly threaten both the world trading system (via their impetus to protectionism) and the health of the international economy itself (via a large and perhaps precipitous fall of the dollar). However, the Fund has been impotent in seeking remedial action. This is true especially in the crucial exchange rate domain, which must make a major contribution to correcting the imbalances, where the Fund's rules—which provide ample scope for initiative—have been totally ignored (see chapter 5 by Morris Goldstein).

The Fund has been totally inactive on the second major threat to global growth at present, the dramatic increase in energy prices, although that topic admittedly lies farther from its traditional purview. Even on issues where it has traditionally led with some success, notably the crisis and

C. Fred Bergsten has been the director of the Institute for International Economics since its creation in 1981. *He is grateful to Jacob Funk Kirkegaard for preparing the tables in this chapter.*

debt problems of emerging-market economies, the Fund has defaulted or made substantial errors, as in its responses to the recent Argentine default and the Asian crises in the late 1990s.

The issue addressed in part II of this volume, and this chapter, is whether reforms in the governance of the IMF itself, and of the broader world economy, can make a significant contribution to strengthening global economic performance. Other chapters in this part make a strong case for substantially reorganizing the "chairs and shares" in the IMF itself, and its procedures for selecting its top leadership, and I strongly support the proposals in those chapters. Such changes would substantially enhance the legitimacy of the Fund and hence improve its prospects for operating more effectively in the future.

But IMF policy on major issues has always been directed by an outside group: the Group of Seven (G-7) since the late 1980s and its predecessor Group of Five (G-5) and Group of Ten (G-10) in earlier periods. A fundamental reason for the increasing ineffectiveness of the IMF during the past decade or so has been the ineffectiveness of its steering committee, the G-7. Reforms are needed in the steering mechanism if the IMF is again to play its needed role as effective manager of the international monetary system, whatever reforms may be made in the structure and operating modalities of the Fund itself.

The ineffectiveness of the G-7 stems in turn from two fundamental causes. The chief problem is substantive. The large, high-income countries have essentially adopted a mutual nonaggression pact under which, facilitated by a global regime of flexible exchange rates and huge international capital flows that enable them to ignore external criticism of their policies, they have simply given up making such criticisms or at least pursuing any serious attempts to alter each other's behavior. The United States, while acknowledging the need to further cut its budget deficits, rejects all foreign critiques of the excessive tax cuts that have been responsible for so much of the problem. Europe resists external advice on both structural changes and expansionary macroeconomic policies that would strengthen its growth. Japan took more than a decade to revamp its banking system and thus restore a foundation for expansion despite atypically aggressive foreign criticism (notably from the United States), and it exacerbated the problem along the way with a series of major macroeconomic policy errors. The G-7 has little credibility in counseling other countries to adopt responsible fiscal and exchange rate policies when it permits huge budget imbalances and massively misaligned currencies to persist in its midst without any serious effort to correct or even address them.

In earlier periods, the G-7 and its predecessors did adopt coordinated and effective responses to very similar problems. In the 1960s, the G-10 resolved a series of exchange rate crises (centered mainly on sterling but also including the dollar and several other currencies) and created special drawing rights in an effort to shore up the Bretton Woods system. In the late

1970s, the Bonn summit worked out a global recovery program with very precise national commitments that was well on its way to success before the second oil shock derailed the world economy. In the 1980s, the Plaza and Louvre accords prevented both a US relapse into system-threatening protectionism and a hard landing for the world economy.

There were failures during these earlier decades too: The G-10, for example, was unable to prevent the breakdown of the Bretton Woods exchange rate regime in the early 1970s. But no such cooperative adjustment program has even been seriously contemplated, let alone adopted, during the present onset of problems that are not only distressingly similar to these earlier episodes but much larger and potentially even more dangerous. A meeting of high officials and academics that I recently attended to discuss these issues reached the profoundly depressing conclusion that there is virtually universal agreement on the diagnosis of the current problem but virtually no possibility of governmental action until after the inevitable crisis hits.

The (Il)legitimacy of the G-7

These substantive hurdles to effective G-7 leadership of the world economy, including the IMF, are increasingly exacerbated by a second problem: the group's exclusion of countries that are essential to resolution of the chief difficulties that must be addressed. The G-7's recent agenda clearly illustrates this dimension of the problem.[1]

First, today's international imbalances require substantial adjustment initiatives by countries outside as well as inside the G-7. China will probably become the world's largest surplus country, even in absolute terms, in the near future (table 13.1) and simply must stop blocking the international adjustment process through its massive intervention in the foreign exchange markets. The economies of Asia, as a group, account for more than 50 percent of the global surpluses that are the counterparts of the US deficit (table 13.1) and must therefore curtail their currency intervention as well. Asian countries have accumulated the great bulk of world reserve increases during the past three years (three-quarters of the total including Japan, almost half excluding that one Asian member of the G-7; see table 13.2). On the policy side, China's unwillingness to revalue significantly constrains the other Asian countries from doing so as well, and their collective resistance to the needed appreciations essentially removes the world's main surplus area from the entire adjustment process.

1. Another key international economic (and social) issue is of course the fight against global poverty, including implementation of the Millennium Development Goals. I view this issue as properly outside the purview of the IMF and join those who, for example, would shift the Poverty Reduction and Growth Facility to the World Bank, so I do not address it in this chapter.

Table 13.1 Current account balances for East Asian countries, 2002–05 (billions of dollars)

Country	2002	2003	2004	2005[a]
Brunei Darussalam	3.1	3.8	4.2	4.6
Cambodia	0.0	–0.1	–0.1	–0.2
China	35.4	45.9	70.0	145.0[b]
Hong Kong	12.6	16.2	15.9	16.3
Indonesia	7.8	7.3	7.3	6.3
Japan	112.6	136.2	171.8	157.2
Korea	5.4	12.1	26.8	26.1
Laos	–0.1	–0.1	–0.2	–0.2
Malaysia	8.0	13.4	15.7	17.4
Myanmar	0.1	0.0	0.0	–0.1
Philippines	4.4	3.3	3.9	2.4
Singapore	15.7	27.0	27.9	27.2
Thailand	7.0	8.0	7.3	3.5
Vietnam	–0.4	–1.8	–2.0	–2.3
Addendum:				
Taiwan	25.6	29.3	19.0	22.6
Total, including Taiwan	237.2	300.5	367.5	425.8
"Share" of US current account deficit (percent)	50.0	57.0	55.0	55.0
United States	–473.9	–530.7	–665.9	–785[c]

a. 2005 data are estimates.
b. Estimate provided by Nicholas Lardy; based on first nine months of 2005 from Chinese customs data.
c. First half of 2005 annualized; obtained from Bureau of Economic Analysis, International Transactions, table 1.

Source: IMF, *World Economic Outlook*, April 2005.

The process point is obvious: The G-7 can hardly expect to forge a coordinated and hence effective response to the global imbalances, even if it wants to, without the full participation of China and preferably several other key Asian countries (at least Korea and India) as well. Inviting one or more of those countries to an occasional G-7 lunch or dinner or even to parts of regular meetings, as has occurred recently, is hardly a substitute for full membership in the club. This is especially true since the whole global leadership issue requires agreed-on diagnosis and mutual understanding of the entire range of international problems, including protectionist pressures and the resultant threats to the global trading system, that are involved.

Second, the G-7 is equally ill equipped to deal with the global energy problem. One dimension of its difficulties in this issue area is that a number of countries that have become major energy importers with a very large impact on world markets, notably China and India, have begun to

Table 13.2 Global foreign exchange reserves, 2001–04

Country/groups of countries	End of year: 2001 (billions of dollars)	End of year: 2004 (billions of dollars)	Change: 2001–04 (billions of dollars)	Change: Share of total (percent)	Percent change, 2001–04
Total					
(173 reporting countries)	1,997	3,688	1,691	100.0	84.7
Asia, total	1,157	2,397	1,240	73.4	107.2
Asia, excluding Japan	769	1,573	804	47.6	104.6
Japan	388	824	436	25.8	112.4
China	212	610	398	23.5	187.7
Taiwan	122	242	120	7.1	98.4
Korea	102	198	96	5.7	94.1
India	45	125	80	4.7	177.8
Hong Kong	111	124	13	0.8	11.7
Singapore	75	112	37	2.2	49.3
Malaysia	30	65	35	2.1	116.7
Thailand	32	49	17	1.0	53.1
Indonesia	27	35	8	0.5	29.6
Philippines	13	13	0	0.0	0.0
Other G-20 members					
Russia	33	121	88	5.2	266.7
Mexico	44	63	19	1.1	43.2
Brazil	36	53	17	1.0	47.2
Turkey	19	35	17	1.0	89.4
Australia	16	34	18	1.1	112.5
Canada	30	30	0	0.0	0.0
Saudi Arabia	15	23	8	0.5	53.3
Argentina	15	18	3	0.2	20.0
South Africa	6	13	7	0.4	121.9
Euro area	208	179	–29	–1.7	–13.9
Euro area opt-outs:				0.0	0.0
United Kingdom	32	39	7	0.4	21.9
Denmark	16	38	22	1.3	137.0
Sweden	13	21	8	0.5	61.5
10 new EU member states	65	114	49	2.9	74.9
Others	292	509	217	12.8	74.4

Sources: IMF, *International Financial Statistics* database, August 2005; Central Bank of China (Tai-

compete vigorously with traditional importers (and each other) for secure sources of supply instead of seeing themselves as fellow consuming countries with similar interests in stabilizing world prices and supply channels. Hence they will increasingly add to the instability of the situation when they should be cooperating with the G-7 countries, primarily through assuming full membership in the International Energy Agency (IEA) at the Organization for Economic Cooperation and Development—which the G-7 should be promoting. Even more important, the G-7 consists primarily of importing countries and could hardly expect to work out legitimate and hence effective solutions that require cooperation and joint leadership with the major oil exporting countries via the Organization of Petroleum Exporting Countries (OPEC).

Third, the G-7 has failed to produce a sustainable and comprehensive solution to the Argentine default, the largest single episode of its type in modern history with potentially huge precedential effects for the management of future debt crises. In the past, the G-7 was largely able to impose its will in such circumstances through its members' control of the IMF and the other international financial institutions. The story has turned out differently this time, at least so far, in part because of the greater weight of the debtor countries—including Brazil, Mexico, and other nondefaulters—in the international economy and financial markets and, thus, the greater weight that must be accorded to their views in reaching a workable solution (either retrospectively or prospectively).

The G-7 is clearly illegitimate to deal with all three of these current (and perennial) headline issues. The global imbalances cannot be seriously addressed without the Asian countries. The energy problem cannot be resolved without all the main importers and without the key producing countries. Debt problems cannot be handled without the chief debtor nations. The IMF will remain ineffectual if its own steering committee is ineffectual. The time has come to recognize that the G-7 will remain ineffective, importantly because it is politically illegitimate, and to replace it with a new steering committee that can infuse the new vision and leadership into the world economy, including via the IMF, that is now so obviously lacking.

Recent developments in the world trading system reinforce this conclusion. The "trade G-20" of developing countries, led by Brazil and India to coordinate the positions of that group at the Cancún Ministerial of the World Trade Organization (WTO) in 2003, successfully and correctly blocked a joint initiative by the G-2 (the United States and the European Union) that would have heralded a meager outcome on agriculture and, thus, in overall terms, for the Doha Round. The rich countries, noting that the poor countries could now get together and exercise veto power over the trading system, have subsequently been experimenting with new steering committees that include the leaders of both groups—most recently a five interested parties (FIPs) group comprising Australia (representing the Cairns Group of food exporters), Brazil, the European Union (which of course negotiates on trade as a single entity), India, and the United States. Faced with the daunting challenge of achieving a successful outcome in their current WTO negotiations, the same rich countries that have been un-willing to create a newly legitimate steering mechanism for macroeconomic and international financial issues have proceeded to do just that for trade policy.

Another reason to create a new global steering mechanism is the prospect of new regional economic institutions, which represent one aspect of the present backlash against globalization and its lead institutions, especially those located in Washington. In particular, East Asian countries are actively negotiating a series of subregional and bilateral agreements in the areas of both money (for example, the network of swap agreements under the Chiang Mai Initiative) and trade (for example, China-ASEAN and Japan-Korea).[2] Extensive subregional arrangements also exist in Latin America (Mercosur and the Andean Pact) and elsewhere (Southern Africa Development Community and the Gulf Cooperation Council) with respect to trade but increasingly with an eye toward monetary and even macroeconomic cooperation as well.[3]

Two implications of this trend are germane for decisions concerning the creation of a new steering committee for the world economy. In the short run, it will be essential to ensure that these new regional and subregional entities are compatible with the existing global rules and institutional arrangements, or that those rules and institutions are amended to encompass the newcomers in an agreed and harmonious manner, or both. The longer-run significance could be even greater. Successful realization of these regional aspirations—especially in Asia, where until recently the integration process has lagged far behind Europe and even the Western Hemisphere—could lead to the emergence of a tripolar world economic structure. Such a construct would encompass the European Union and its neighboring associates, a Free Trade Area of the Americas (or perhaps a NAFTA and an expanded Mercosur that were loosely linked), and an East Asia free trade area–Asian monetary fund. In such a world, a global steering committee that included the key players from each of the three regions—including China and Korea as well as Japan in East Asia and Brazil and perhaps Argentina in South America—would be of cardinal importance in managing relations among the regions, which would in turn be central for global harmony and stability.

The prospect of such a tripartite world, which is quite possible over the next decade or even less, provides a powerful additional rationale for the proposition that a broader grouping should supersede the G-7 as the informal steering committee for the world economy. The G-7 would be even more inadequate for that task in a world where not only its share of the world economy continued to decline substantially but leaders of key regional arrangements were outside the group.

2. ASEAN is the Association of Southeast Asian Nations.

3. Mercosur is the Mercado Común del Sur (Southern Cone Common Market).

The Reform Options

Any new steering committee must seek to find the optimum trade-off between legitimacy and efficiency. It must be sufficiently representative to encompass all relevant sides of the key issues and thus be acceptable to the many parties that will inevitably remain outside the inner club. But it cannot be so large as to be unwieldy and incapable of action. To take the extreme cases, a G-2 of the United States and the European Union (or even more so a G-1, which the United States is sometimes called) would obviously be illegitimate while the UN General Assembly (or the full membership of the IMF, which is only a little smaller) could never be expected to initiate decisive actions.

The first option for reform lies at the maximum-efficiency end of the spectrum: replacement of the G-7 with a Group of Four (G-4) comprising the United States, China, Japan, and a single representative of Europe.[4] Such a group would have balance both geographically and ethnically. It would include one developing country (with a population that substantially exceeds the combined population of the three rich members). It would include the four largest economies in the world (at purchasing power parity exchange rates) that are hence most responsible for most macroeconomic and monetary issues. New members, most likely India over the next decade or so, could be added as their global economic importance rose to sufficient prominence.

The second option would build on the existing G-7 to include the BRIC (Brazil, China, and India as well as Russia, which already participates in Group of Eight [G-8] summits); South Africa, to provide representation for Africa; and perhaps Mexico. These five countries have already been invited to participate in parts of several recent G-8 summits and meetings of G-7 finance ministers. Such limited representation is obviously inadequate, relegating the invitees to second-class citizenship. A full-blown G-12/13 (or 8 + 4/5, as it is sometimes called) would have the virtue but also the shortcoming of building on an existing institution as it sought a balance between efficiency and legitimacy. Reducing European representation to one in this context would shrink the configuration to a more manageable G-10/11. The group would be evenly divided between rich and poor, and between Caucasians and non-Caucasians. All regions would be represented except the Middle East (or indeed any Muslim-majority country) and the Southwest Pacific (which is sometimes viewed as part of Asia and sometimes not).

The third option would build on the existing Group of Twenty (G-20), which has been meeting at the level of finance ministers and central bank

4. Until the United Kingdom joins the euro, this would probably require representation by the full European Union at the summit level and representation by Euroland in the Finance G-4.

governors (and their deputies) since 1999. This group would add six more countries: Argentina, Australia, Indonesia, Korea, Saudi Arabia, and Turkey.[5] The additions would include several oil exporters, including the most important one, and three major Muslim countries. Because the European Union is already counted separately, the group could be slimmed to a G-16 by dropping the four individual European countries.

One crucial political factor must be addressed before choosing among these options. The G-7 has come to refer to itself in recent years (though not at its outset) as a group of "leading industrial democracies." Russia was admitted to the annual summits, though only marginally to the finance ministers' meetings, in the early 1990s as a reward for becoming a democracy.[6] Much of the resistance to China's addition to the G-7/8, particularly in the United States, has been based on the continued authoritarian nature of its political system. Similar questions could be raised about Saudi Arabia, which (like China) is nevertheless already a member of the G-20.

Decisions on future global governance thus need to address squarely the purpose of the exercise. Is it to manage the world economy effectively, in which case the economic criteria emphasized in this chapter should predominate? Or does it have broader purposes, both symbolizing the "club of democracies" and holding out an incentive for countries to adopt major political as well as economic reforms? Because China is both the obvious "next member" of any of the new groupings on economic grounds and the most controversial case politically, this debate might block otherwise desirable reforms for considerable additional time.

A possible resolution is to distinguish explicitly between the summit and finance ministers' levels of the potential new groupings. The Finance G-7 could become a Finance G-20 (or some variant thereof) while the Leaders' G-8 would remain just that, perhaps with ad hoc invitations to nonmembers as at present. Such distinctions have already existed for considerable periods, most recently since Russia began attending summits in the early 1990s (but the Finance G-7 [F-7] only sporadically) but also when Canada and Italy were added to the summits in the middle 1970s but not to the finance group until a decade later. There is clearly no need for precise equivalence in the membership of the groups.

The most pragmatic way to proceed to a more effective steering group for the world economy, especially now that the summits focus so heavily on political issues and usually remand the major economic topics to their

5. The European Union is counted as a separate member additional to the individual European countries when the presidency of the European Union is not held by one of the four individual EU members of the group; this is unlike the European Union's treatment in the G-7/8.

6. Spain, Portugal, and Greece were admitted to the European Union after they became democracies.

finance ministers anyway, is thus to revamp the meetings of the latter and await future political developments to enable the summits to catch up. There would be some cost in not moving at the leaders' level as well because only the leaders can make effective interissue trade-offs between, for example, energy policy and macroeconomic policy as at Bonn in 1978. In addition, the country that chairs the annual summits has recently come to play an important role in steering the work of the Finance G-7 so there is some linkage between the substantive activity of the two groups. Moreover, some countries (China?) may be less likely to cooperate at the finance level—or even be willing to join that group—if they are not included in the "parent organization" as well.

However, the summits have become even more ineffective than the Finance G-7. As noted, they have taken to remanding most of the economic issues to the latter in any event. Hence the most promising prospect for renewed economic leadership probably lies with the ministers, and priority should be given to restoring their legitimacy. Significant success from a reformed Finance G-7 could in fact provide a stimulus to similar future evolution of the summits themselves.

Another political issue that cuts across all the reform alternatives, within the Fund as well as for the steering committee, is the representation of Europe. Europe simply cannot continue having it both ways: insisting on both equal treatment with the United States as an economic superpower and multiple representation in all the international economic bodies. Lorenzo Bini Smaghi (chapter 10) and other thoughtful Europeans have made the case for consolidating the EU (or Euroland) position, which is essential to permit the needed changes in chairs and shares at the Fund and would be of enormous assistance in facilitating any of the proposed reforms of the steering committees.

The most promising grouping for steering committee purposes for the foreseeable future is a modified Finance G-20, eliminating the four individual European countries (including the United Kingdom) in favor of Euroland alone and thus creating a Finance G-16 (F-16). Such a group would comprise about 80 percent of world output (table 13.3). It would represent all regions, cultural groups, and income levels. Its members would have the competence to address every major issue facing the world economy. Hence it would offer a much more promising basis for steering the world economy and its formal institutions, including the IMF.

An alternative steering mechanism that might be considered for the IMF itself is the International Monetary and Financial Committee (IMFC), which replicates the Fund's Executive Board at higher political levels and is in fact supposed to play just such a role. It has existed for some time, however, mostly under its inglorious former title of Interim Committee, and has never effectively done so. That failure is typically ascribed to numerous technical reasons, including the presence of far too many countries (included in the 24 constituencies) and people in the room as well as

Table 13.3 Economic size of selected countries and groups of countries, 2004

Country/group of countries	GDP at market exchange rates: Billions of dollars	GDP at market exchange rates: Percent of world total	GDP at PPP exchange rates: Billions of dollars	GDP at PPP exchange rates: Percent of world total	Share of world population (percent)
G-7	25,929	63.8	23,946	43.0	11.1
United States	11,733	28.9	11,605	20.9	4.6
Japan	4,668	11.5	3,817	6.9	2.0
Germany	2,707	6.7	2,392	4.3	1.3
Britain	2,126	5.2	1,736	3.1	0.9
France	2,018	5.0	1,725	3.1	0.9
Italy	1,681	4.1	1,620	2.9	0.9
Canada	996	2.4	1,050	1.9	0.5
EU-25	12,702	31.2	11,724	21.1	7.1
Euro area	9,398	23.1	8,501	15.3	4.8
China	1,649	4.1	7,334	13.2	20.5
India	661	1.6	3,291	5.9	17.1
Brazil	600	1.5	1,462	2.6	2.9
Russia	583	1.4	1,449	2.6	2.2
Mexico	676	1.7	1,005	1.8	1.7
South Africa	213	0.5	502	0.9	0.7
Indonesia	258	0.6	801	1.4	3.7
Turkey	300	0.7	530	1.0	1.1
Korea	681	1.7	1,030	1.9	0.7
Argentina	152	0.4	484	0.9	0.6
Saudi Arabia	249	0.6	316	0.6	0.4
Australia	618	1.5	602	1.1	0.3
G-4, with EU-25	30,753	75.6	34,480	62.0	34.1
G-4, with Euroland	27,449	67.5	31,258	56.2	31.9
G-7, plus BRIC, South Africa, and Mexico	30,311	74.5	38,988	70.1	56.1
G-7, including all EU-25, plus BRIC, South Africa, and Mexico	34,482	84.8	43,239	77.7	59.2
G-7, including all Euroland, plus BRIC, South Africa, and Mexico	31,178	76.7	40,016	71.9	56.9
G-20, including all EU-25	36,740	90.3	47,003	84.5	65.6
G-20, including euro area	33,435	82.2	43,780	78.7	63.8
World	40,671	100.0	55,655	100.0	100.0

BRIC = Brazil, Russia, India, and China
EU-25 = membership of the European Union after 10 countries were added in 2004
Euroland = countries that have adopted the euro as their currency
G-4 = Group of Four (United States, China, Japan, and a single representative from Europe)
PPP = purchasing power parity

Note: Groupings that include the euro area do not include Great Britain.

Sources: IMF, *World Economic Outlook*, April 2005; UN Statistics Division.

the group's being captive to IMF management and staff. Its main problems, however, are those that have plagued the other groupings described here: the gross overrepresentation of Europe and underrepresentation of Asia and, hence, fundamental illegitimacy of its construct; and the unwillingness of the real steering committee of the overall world economy to let this subsidiary body play a meaningful role.

Evolution or Big Bang?

Most reform proposals assume that any new grouping, such as the proposed F-16, would evolve alongside all the existing groupings—including those it would be supplanting in leadership terms, in this case the G-7 (and, to the limited extent it is still relevant, the venerable G-10). This has indeed been the historical norm although the G-5 did finally disappear after holding out for several years despite a directive from the Tokyo summit in 1986 to add the two G-7 countries (Canada and Italy) that had been attending summits, but not their finance counterparts, for a decade.

It is unlikely, however, that a new F-16 could truly seize the required leadership mantle if the F-7 continued to exist. Healthy and productive competition between the two groups is a theoretical possibility. With such a large and overlapping membership, however, there would be too much incentive for the incumbent F-7 to maintain control, and it could easily block the F-16 from taking any serious actions or even addressing the key issues (as the G-5, even while in the process of dissolving, continued to meet and make the major decisions—as at the Louvre Summit in 1987—before the subsequent sessions of the G-7). There might also be understandable hesitation on the part of the fledgling F-16 to assert authority. The likely result would be even poorer leadership than at present, with each group simultaneously seeking to protect its turf and fob off the toughest issues on the other (including to make the competition look bad by failing to work out effective resolutions).

Except for the proposed change in the status of European representation, the F-16 already exists. Hence the only decision needed to alter the global economic governance structure in the proposed manner is for the F-7 to declare its dissolution in favor of the broader F-16, a natural follow-on step to its decision to create the G-20 in the first place. The decision would be a voluntary act by each country to end its participation in an informal international club, requiring no signing of treaties or appropriation of funds. It would require no congressional, parliamentary, or other domestic approvals in the member countries. I thus recommend that the world move to sole reliance on a new F-16 as soon as possible to provide the steering mechanism for the global economy that is so crucially needed, including the leadership and direction for the IMF that is essential for it to become a strong and effective institution once again.

What Difference Would It Make?

Reform in the governance structure of the world economy, including in the IMF itself and in the systemic steering committee, is a necessary step toward improving the prospect for effective leadership and thus better global economic performance in the future. It is clearly not a sufficient step, however. National governments will still have to decide that it is in their interest to cooperate internationally to a much greater degree than in recent years, recognizing anew the sizable repercussions on their own economies of the external impact of their domestic actions and the virtues of adopting the slightly longer time horizons required to enjoy the payoff from cross-border collaboration.

The new F-16 governance structure could help considerably, however, in addressing the three important international economic issues described above that have not been handled effectively by the G-7 (and the IMF).

The case for improved performance is easiest to envisage in the case of the global imbalances. In discussions in which they were full participants, China and the other Asian countries would now be asked, by the European countries and other developing countries as well as by the United States, to adjust their exchange rates and begin relying much more heavily on consumption-led rather than export-led growth. They could therefore, in those same discussions, push the deficit and debtor country—the United States—to make its requisite major contribution to the global adjustment by substantially raising its national saving rate (by whatever measures it deemed most cost-effective). The United States, along with the Asian countries, could at the same time push Europe to boost its lagging growth rate by whatever combination of structural and macroeconomic measures it deemed most appropriate.

It is in fact not difficult to imagine the contours of a package of specific commitments, whose implementation would be monitored closely by the deputies, in which the three main regions agreed to adopt the steps that are necessary in each to achieve a smooth and orderly, rather than a financially disruptive and trade restrictive, adjustment of the large and growing international imbalances. It is also quite conceivable that each government would more easily be able to convince its domestic constituencies of the merits of taking the needed actions in the context of such an international agreement, where the partner countries were fulfilling their responsibilities in a way that made all the parties better off. The demonstrable benefits of policy cooperation would now be apparent to a wider group of countries, including virtually all those needed to carry out the necessary action program, and thus the prospects for constructive behavior would be much greater.

Similar scenarios could evolve with respect to the energy issue. An F-16 could institute a meaningful conversation between key producing countries (especially Saudi Arabia) and key consuming countries (especially the

United States and China) that would deepen realization of the disruptive impact of the huge price swings—down as well as up—that have characterized the oil market for more than three decades and, thus, the need to develop a new energy regime. Any negotiations toward such reform would of course have to include a much broader group of countries, presumably centered on OPEC and the IEA (which, it is hoped, will be expanded to include China, India, and other key developing importers), but the Leaders' G-16 (L-16) might be able to steer the process here as elsewhere.

On international debt and other direct IMF issues, an effective L-16 could institute less dramatic but still important steps. As a starter, it could agree to increase IMF quotas to provide the basis for altering chairs and shares, as recommended by Truman (chapter 9).[7] The F-16 could thus contribute immediately to enhancing the legitimacy of the Fund and indeed to restoring support for it in parts of the world that are now disaffected from the institution. With all the main creditor and debtor countries in the room, but with a manageable number of participants, it could also have a balanced debate on the lessons from Argentina and attempt to set new Fund policy to both complete that current episode and prepare for similar cases in the future. A model for the new F-16 could be the original G-10, which was created in the early 1960s to help finance the US and British balance of payments deficits of the day (via lending to the Fund to augment its own resources) and also included both lending and borrowing countries.[8]

Governance reform is no more a panacea for the present shortcomings of the IMF, and for global economic management more broadly, than any of the other changes suggested in the papers for this conference. In combination with some of those substantive changes, however—in particular those proposed by Morris Goldstein (chapter 5) and John Williamson (chapter 6)—it could produce a significant improvement in the functioning of the Fund and the system as a whole. Governance issues, including at the systemic level, deserve a central place on any future IMF reform agenda.

7. It could do so either within the current quinquennial review, which is scheduled to terminate in 2008, or by extending that period by another year or two to permit more time for a decision.

8. I am indebted to Ted Truman for pointing out this analogy.