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Opening Remarks

Subcommittee on International Monetary Policy and Trade Hearing

"Implications of the G20 Leaders Summit for Low Income Countries and the Global Economy"

May 13, 2009

On April 2, 2009, the leaders of the G20 nations gathered in London to address the global financial crisis which has gripped nearly every nation in the world. The resolution put forward by the leaders was broad and far reaching, both in its scope as measured by the actions proposed, but also in its inclusion of nations which we may have been tempted to ignore in the past. Indeed, the very fact that the meetings in London were of the G20 leaders, plus representatives from other key emerging economies and international financial institutions, is a testament to the global nature of the crisis, and the imperative of a global approach to the solution.

But the question remains as to why, when we are faced with the deepest economic and financial crisis since the Great Depression, we should allocate time, energy and resources to poor and emerging economies, beyond our usual aid and humanitarian activities. I believe that, beyond the altruistic reasons for assisting poor and emerging countries, we have strong business, economic, and geopolitical reasons to follow-through on the commitments made by President Obama and the other leaders at the G20 Summit.

Indeed, it is critical to note that when we are not present, either directly through bilateral assistance, or indirectly through international financial institutions and multilateral development banks, others step in to fill the void. To do nothing and look the other way is in fact to do something. When we decide to walk away from our obligations under the pretext that the crisis is too severe to help others, we open the door for others to step in and fill the void we create. This is not just a theoretical threat, but in fact a very real one. Institutions like the IMF, the World Bank and many others which America supports and which were mentioned as critical to global economic recovery in the G20 communiqué act as balanced mediums to provide countries in need with much needed resources to forestall crisis, while moving these same countries to more stable, more sustainable, and more peaceful paths to economic growth. This is something we should all support.

We have called this hearing to follow-up on the G20 resolutions, endorsed by President Obama, which made explicit the importance of not just providing aid to those nations and communities in the most dire need, but rather to include poor and emerging economies as full participants in any strategy to pull the global economy out of recession. The wording of the G20 communiqué made this explicit. The reasons for following through on the commitments made by President Obama and the other leaders at the G20 Summit in London can be broadly grouped into three categories:

1) Supporting American industry

2) Preventing further systemic risk in global capital markets and encouraging continued sound economic reforms

3) Promoting socio-political stability

Addressing these issues in order, I will begin by discussing the impact on American industry. As the G20 communiqué stated, emerging economies have been a true engine of global economic growth in the recent past. As we saw with the Asian financial crisis of the late 1990s, when the emerging economies of Asia stalled, world economic growth stalled. When the financial crisis that struck Asian economies was resolved, the world as a whole resumed on a path of rapid economic expansion. In many ways, we face a similar crisis today, on a much larger scale. As our economies have become increasingly inter-dependent through trade and vertical outsourcing, American producers are directly and indirectly exposed to consumers and manufacturers around the world. Driven by their rapid economic growth, emerging middle classes, and young populations eager to consume American goods and services, emerging economies have become major consumers of goods and services produced by American companies. As a result, many American companies stand to gain from our efforts to support the continued economic growth in these countries. As was the case with the Asian financial crisis, restarting the engines of growth in emerging economies will be a critical component to restart our own economy here at home.

Looking at the second point, about preventing further systemic risk in global capital markets, it is important to revisit some important changes that occurred in the past decade or so. It has been well documented that, following the Asian financial crisis and the Argentina crisis earlier this decade, the IMF experienced a dramatic drop in its lending activities around the world. This was in part due to what was seen as overly harsh conditionality on loans and stigma associated with turning to the IMF for balance of payment assistance. But this was also largely due to the availability of other sources of funding for many emerging market governments. Indeed, as capital markets matured and expanded aggressively to the four corners of the world, companies and governments in emerging markets found themselves able to borrow from global banks, investment funds, and alternative investment vehicles like never before. This enabled many of these countries to pursue their economic development strategies while building up healthy reserves. Where the debt stock of poor and emerging economies would previously have been constituted nearly entirely of IMF, World Bank, and other international development institution debt, increasingly banks and investment funds accounted for a large share of that debt. This, of course included American investors and American banks. As some of these debts come due, many countries will be unable to meet their financial obligations, creating the very real risk of another wave of bank failures and a further retrenchment of credit, internationally, but also here in America.

This risk of default, primarily on sovereign debt, but also by the largest companies in these emerging economies, is equally true in countries that followed what would be considered sound macroeconomic policy, building up healthy reserves and investing in the development and diversification of local industry. This is true because of the nature of the crisis they are facing. They are dealing simultaneously with falling demand for their exports, a steep fall in commodities prices, collapsing remittances, drastic reductions in international aid, rising domestic unemployment, and returning emigrants. Even the best prepared emerging economies cannot withstand such a confluence of negative shocks at once, and risk severe balance of payments pressure. To make credit available to these economies through institutions like the IMF, allowing them to roll-over their debts and continue to meet their domestic and international financial obligations, is to protect global capital markets, including American banks and investors, from another series of systemic shocks that could bring global credit markets to a near halt.

As described, many poor countries and emerging economies have implemented sound macroeconomic policies in the past decade or more. This of course has not been universally true, but evidence abounds of countries in Africa, Asia, Eastern Europe and Latin America applying more conventional, trade-driven, free markets policies. These countries have reversed long trends of nationalization of industries, choosing instead to foster entrepreneurship and competition, opened their economies to international trade, and put in place the foundation of good governance. To fail these nations now, by not supporting their continued efforts of reform, is to risk reversing a decade or more of economic achievement.

The third topic, socio-political stability, should be top of mind to all nations seeking a way out of this global financial crisis. Simply put, we are at an inflection point in history, and our decisions in the coming weeks and months will define the future path of global economic growth and broader geopolitical events. As already explained, many poor and emerging economies face a perfect storm of external shocks which is putting a great strain on their economies, both at the macroeconomic level, but also at the microeconomic level. Emerging economies and fragile democracies will be severely tested by collapsing demand and prices for their exports, rising unemployment, falling remittances, and unemployed migrants returning to their home countries. If nothing is done, these and other factors will inevitably push some countries to civil unrest, if not outright war. It is in the interest of all peaceful nations to ensure that this be avoided. As we approach this inflection point in history, and accept that to do nothing is not an acceptable option, we now consider how our actions can set emerging countries on a path to sustainable, peaceful growth, sowing the seeds of freedom and democracy in regions of the world where they have been elusive. Trade finance and a rejection of protectionism are critical components of the G20 resolutions. But the details were lacking, and present a great opportunity for us to put our imprint on the nature of this recovery, and the structure of future economic relations between rich and poor nations of the world. As we follow-through on the commitments made at the G20 Summit, we can and must focus on capacity building in emerging markets, to make them full participants in a sustainable, open and fair system of global trade. The alternative is no longer acceptable, as it leads to instability and open conflict within and between nations. As Frédéric Bastiat, a 19th century French economist rightly said, “when goods don’t cross borders, armies will”.