Tackling the challenge of global governance reform

By Shada Islam

Two years ago at their meeting in Beijing, Asian and European leaders vowed joint action to rebuild the battered global economy. "We swim together, or we sink together," European Commission President José Manuel Barroso told the ASEM summit. Can that message of solidarity and pledge of collective action be repeated again when Asia-Europe leaders gather in Brussels on October 4-5?

The good news is that Asian countries have weathered the crisis much better than anticipated. China, India and several members of the Association of Southeast Asian Nations (ASEAN) are notching up impressive growth rates. Fiscal stimulus packages agreed by countries across the region have helped bolster the world economy. Significantly, China recently decided to end the yuan's peg to the dollar, thereby helping to boost the competitiveness of Western companies. The move also helps avoid overheating of the Chinese economy and helps correct global imbalances.

European countries appear to be on a more subdued trajectory. Faced with the debt crisis in Greece, European Union finance ministers in May and June had to agree a rescue mechanism worth around €750 billion to safeguard financial stability in the euro area as well as take action to ensure fiscal sustainability. Acting to reform economic governance in the euro zone, EU countries are introducing closer economic surveillance, with an early peer-review system aimed at preventing a repeat of the Greek sovereign debt crisis. Germany, Britain, Italy, France, Spain and Greece are also cutting spending to reduce their high deficits in a bid to promote stability and restore market confidence.

The US, Japan, South Korea and Japan, countries which want to maintain stimulus spending to boost growth, are critical of Europe's spending cuts. At the recent meeting in Canada, leaders of the Group of 20 (G 20), representing major industrialised countries and emerging nations also disagreed over plans by Germany, France and Britain to impose bank taxes to recoup bailout costs. Despite the discord, however, the final G20 communique managed to strike a delicate balance between restoring budget discipline and sustaining growth. It also said countries will be given a choice whether to levy taxes on banks and could phase in stricter bank capital rules to fit national needs.

Despite the difficult public debate, Asia and Europe face a common challenge of crafting a new growth model for the global economy.

In Europe, wide-ranging structural reforms are needed to improve access to finance for research and development, to facilitate the entry of young people on the labour market, improve the business environment, especially for small and medium-sized businesses and enhance the efficiency of financial markets. Asian governments, meanwhile, must widen their modest social safety nets, allow currencies to appreciate, deepen regional integration and reform financial markets to allow for a more efficient allocation of credit. Asian nations must also take measures to boost domestic demand, thereby scaling down their dependence on exports.

The crisis, in fact, provides an opportunity to move ahead with much-needed reform of the international economic and financial architecture. Action needs to be taken to tackle current weaknesses in macro-financial surveillance and policy coordination as well as in the financial regulatory and supervisory framework. There are also deficiencies in crisis management mechanisms of the International Monetary Fund and multilateral development banks. Most significantly, the crisis has highlighted the need to overhaul global economic governance.

The G20, undoubtedly an important innovation in global governance, reflects an ongoing shift of global economic and political power to the developing world - particularly to Asia. It is the only international forum in which major developed and developing nations meet in formal equality at the highest level of government. As such, it offers a framework to encourage emerging powers to accept new responsibilities.

G20 leaders have scored important successes. At their summit in London in April last year, the leaders mobilised $5 trillion to help reassure markets. They restored confidence in the IMF and created a Financial Stability Board to strengthen global regulatory standards. The meeting also held the line against protectionism, preventing a 1930s-style trade war.

Important challenges remain, however. There is a risk that the group will fall into oblivion after the crisis and its unclear membership and operating rules – and marginalisation of those outside the club – could harm its credibility. Meanwhile, with four European countries as well as the presidents of the European Council and the European Commission attending G20 meetings, the EU is under pressure to streamline its membership.

Europeans also face the challenge of accepting reform of IMF governance to reflect the rising economic power of Asian and other countries and to tackle the issue of their representation in the organisation.

China, India and other emerging countries are demanding more seats and more voting rights at the IMF and the World Bank. The G20 has agreed to increase developing countries' voting power in the World Bank and the IMF by at least three percent and five percent, respectively, in a bid to improve the legitimacy and effectiveness of both international institutions.

The World Bank Development Committee has, in fact, responded by raising developing countries' voting power by 3.13 percentage points to 47.19 percent. The debate on changes in the IMF is more acrimonious.

European Commission President Barroso has said Chinese and Indian calls for IMF reform are reasonable. He has also come forward with suggestions that the EU should have one consolidated seat in the Fund, a move that would give Europe more leverage in policy debates on the global stage. However, many European countries remain reluctant to make the required "sacrifice."

Delaying the inevitable makes little sense, however. With the financial crisis injecting more momentum into the power shift from the West to Asia, it is clear that restoring global economic confidence will require joint efforts by the EU, US and Asia's rising powers. However, it is no longer enough to pay lip service to the changes wrought by globalisation. Europe and America must get used to sharing power with the newcomers and accept that emerging actors will have their own ideas on refashioning global institutions.

The ASEM meeting in October provides an opportunity for a much-needed frank and open dialogue among Asian and European leaders on re-adjusting global governance and up-dating old-fashioned mindsets. Both Asia and Europe say they believe in effective multilateralism. They should turn those words into action.

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Note: **ASEM** was launched in 1996 as an informal forum for discussion between Asian and European countries. The current ASEM partners are: Austria, Belgium, Brunei Darussalam, Bulgaria, Cambodia, China, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, India, Indonesia, Ireland, Italy, Japan, Laos, Latvia, Lithuania, Luxembourg, Malaysia, Malta, Mongolia, Myanmar, Pakistan, Poland, Portugal, Republic of Korea, Romania, Singapore, Slovakia, Slovenia, Spain, Sweden, Thailand, The Netherlands, The Philippines, United Kingdom, Vietnam, the ASEAN Secretariat and the European Commission.

Shada Islam is a journalist in Brussels with a long experience of EU-Asia relations. This is a part of a series of articles being published by "Particip" an independent, internationally-recognised consultancy, which is under contract to the European Commission, to look at different aspects of the multi-faceted Asia-Europe relationship. Other articles of the series can be found on the ASEM 8 website: http://www.asem8.be/related-documentation. This article represents the views of the author.