

Don't expect much from the G-20 Summit

As you will be reading this, the G-20 summit in London is underway. This is a summit that Anne Applebaum, (Slate Magazine's columnist, Pulitzer prizewinner and privately the wife of Poland's foreign minister) has dubbed "something that is loud, unnecessary and costs \$75 million"! It is difficult not to agree with her when you consider that these leaders come to London to tackle difficult global issues during a meeting that lasts one day! Indeed, to make it easier for the leaders, the host - UK has prepared a draft communiqué that the leaders will sign on Thursday at the close of the meeting. Of course, that is if they agree!

But when you look at the draft communiqué that is available on the website of the Financial Times, a number of issues come to my mind:

The leaders will have to tackle the issue of **stimulating the economy** so as to create new jobs. In the communiqué, it is written that the efforts so far have created 20 million jobs. But then, the stimulus packages have been undertaken by the USA and UK. Other major countries like France and Germany are weary of implementing such stimulus packages. There are two major reasons for this: Europe thinks that such a package will not stimulate the economy and secondly, and above all, EU countries have to adhere to strict fiscal spending limitations, generally known as the Maastricht Criteria. Therefore, Europeans cannot borrow as much as they wish, unlike in the case of USA or UK.

The leaders are optimistic and expect global economic growth to start by next year – 2010. They expect this **growth to be fuelled by fiscal stimulus**. This is a return to fiscalism and government intervention – something that the World has been despising over the last twenty years or so. This fiscalism will be limited in the EU as countries will have to adhere to the Maastricht Criteria. What about the other countries like China and the BRICs? China and BRICs will come to London with the intention of changing the global economic power distribution, especially that they wish to have greater influence on global economic affairs. To show how determined these countries are, one has to remember last week's words from the Brazilian president Lula daSilva –who said that "the current crisis was caused by blue-eyed people who thought that they were intelligent. Now they are asking us to bail them out!" I think there is a bit of racism here. On the other hand, China is looking for a **replacement of the dollar as a global currency**. The question is: Which currency will take over the US dollar? The Chinese are suggesting the SDR – the IMF virtual currency whose value is expressed as a composition of the dollar, pound, euro and yen. What about the Chinese renmbi? These and many other differences are simply suggesting that at the end of the day, fiscal stimulation of the economy will fall on deaf ears!

The leaders propose to **give the IMF more money** and thus, these funds would be borrowed to countries face hardships like Iceland, the Baltic States, Hungary and various Developing Countries. The issue here is to fund the IMF to a tune of \$500 billion. The question here is who will put up these funds? Considering that the USA, UK and EU are in recession and need

funding, the only option is to ask those countries with excess cash. These are oil-exporting Gulf States and Norway. But what do you give these countries in return? A permanent seat in the Security Council or become part of G-8 so that it increases to G-10?

The communiqué goes on to state that critical to further global development requires **helping developing countries**. The mistake here is that this help will be in line with the so-called Millennium Development Goals – a set of mystic and blurred goals to be attained by 2030 or 2050!! The problem here is that those financing the MDGs will dictate how this money is used and basically, it means developed countries, exporting their unemployed to developing countries. Therefore, expect developing countries will come back from this summit, empty-handed.

Finally, the communiqué contains a number of measures aimed at correcting and improving the global financial market. Basically, the proposal involves the introduction of more stringent regulatory activities and pumping tax-payers money into the system. My problem so far this has been applied and what the banks have done is to “sit on this money” and/or pay it to the bosses as perks!. Banks cite lack of trust in the system for them to give out this money as loans. Therefore, further cash infusion will not improve the situation in the banking system and therefore, not solve the problem.

I am of the opinion that the current global crisis originated from the USA and therefore, solving these problems must start from the USA. But this does not mean infusing trillions into the banking system but rather, removing the defaulted debt – the very first reason why we got into this crisis!. This can only be achieved by forgiving debt of those who borrowed the money – the folks in Main Street! In this way, the toxic instrument that created the poison that was later on, transmitted throughout the global financial system is going to be neutralized. The cost is not as huge as that money that has already been pumped in the system: assuming that the average mortgage size in the USA is \$300 000 and according to *CNN-Money* “a total of 1,081,395 homes have been lost to foreclosure since the housing crisis hit back in August 2007”, this means that the money to clean the system, must be at least \$324,4 billion. This is roughly half of what Sec Polson had pumped into the banking system at the end of the Bush Administration. Without any results! Further, data from the Mortgage Bankers Association of America, shows that outstanding multifamily debt stood at \$890 billion in the second quarter of 2008. This is much lower than what has so far been totally pumped into the system and/or trying to save the auto industry.

As we can see the USA has the appropriate money to wipe out the debt and thus, the toxic instruments in the financial system. This would be the starting base for cleaning the financial system because the borrowers would be cleared of any debt and their credibility dramatically improves to further stimulate the economy; secondly, the banks receive money to clear the outstanding debts and this improves the bank's position on the interbank market. Thirdly, with the guy in Main Street cleared, he can start new activities and purchase products; in this way stopping the further spreading of the crisis. The final stage of

“cleaning” the system would involve removing the liabilities created by virtual financial instruments created at the height of the boom in 2006 - 2008. However, only tangible instruments like bonds or CDs can also be cleared in a similar way.

Without such a grass root solution that will solve the problem at its root cause, do not expect much from the London G 20 Summit, especially that each and every leader will take this opportunity to show his home audience that he has fought very hard to achieve the best for his country, especially the French and the Germans.

Dr Richard Mbewe