

JEFFRY FRIEDEN

Professor of government at Harvard University

I am Jeff Frieden and I am reporting on the proceedings of the workshop on the state of the world economy and finance, under the able tutelage and chairmanship of Jean Claude Trichet. We had a lively discussion and some were reluctant to leave after the allotted three hours. It covered a range of topics on international financial and especially economic affairs. We started by noting that there are very substantial risks in the international economic order today.

The first and perhaps the most striking and worrisome is continued stagnation in Europe, where the crisis continues to affect both economic activity and financial stability. There is grave concern both within Europe and around the world. This is about the near term future of the European economy and about the long term implications of economic difficulties in the European economic space. The second and broader concern and source of risk in economic activity is that we see the continued potential for macro economic imbalances, which have not gone away. China just marked its largest single monthly current account surplus and the German surplus remains large. These macro economic imbalances are to some extent exacerbated by large scale capital flows, which can be destabilising in certain circumstances.

Overall, there was a consensus. We have not found a full range of appropriate tools to deal with the international financial system. We cannot deal with the ability of an integrated financial system to provide the full benefits that it can offer to the world without incurring very serious risks. These include risks we have observed in the last few years. It was also observed that bad behaviour and unacceptably high levels of executive compensation in the financial system risk creating a backlash within the mass public. This would make the task of stabilisation and making full use of the benefits of international financial integration even more difficult. Those are some of the risks that we identified in the course of the workshop.

However, we also noted that there has been serious progress on many fronts, especially with regard to the harmonisation of financial regulatory standards and related issues. There has been some substantial success in both agreeing upon and implementing Basel regulatory standards with respect to liquidity ratios and leverage. There have been similarly important achievements, such as those discussed around the recent Brisbane G20 Summit, as reported, influenced and overseen by the Financial Stability Board. This is especially concerning efforts to stabilise and systematise the evolution of systemically important financial institutions.

Also, on a more positive note, at least one of us waxed enthusiastic about the prospect of Abenomics in Japan. We all recognise that further action is needed in the international financial and economic space. This is particularly with respect to non banks and the shadow financial institutions, which have caused such great difficulty in the last few years. With respect to credit rating agencies, their role in international financial affairs still remains puzzling. We also discussed the harmonisation of accounting standards.

I would say that overall, the feeling of the panel in the workshop was that the news is mixed. There have been some notable steps forward in cooperative measures among the major financial and economic centres, especially with respect to the harmonisation of financial regulation. At the same time, the global macro economic situation remains quite troubled and quite troubling, with Europe being the most worrisome cause for concern.