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# Global Governance After the COVID-19 Crisis<sup>1</sup>

M. Larionova, J. Kirton

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## Abstract

*Assessment of the impact of COVID-19 on international institutions and international relations is essential for shaping global governance for the post COVID crisis world. The authors review the actions of the key international institutions in response to the pandemic undertaken in January-March 2020 reflecting on three questions. First, were the actions undertaken by the international institutions adequate, coordinated and timely? Second, could the outbreak have been contained if the global governance system was not in a state of severe strain, with many of the gaps exposed and reforms promised in the wake of the 2009 financial and economic crisis unfulfilled, its key causes unaddressed and unilateralism rising among its key members? In addition, was the COVID-19 crisis exacerbated by the crisis of multilateralism? Third, and most difficult, what is the future of global governance after the COVID-19 crisis ends? The analysis of international institutions performance three months into the crisis leads to authors to conclude that there have been inadequate actions to produce a timely, coordinated international response from all the major multilateral organizations and from the newer plurilateral summit institutions of the BRICS, G7 and G20. The failure of these global governance institutions was due not only to the severe strains from leading members' unilateralism and competition, but from the very architecture designed in 1945 that now poorly matches intensely globalized world. Global governance in the post COVID world should not descend into the old war-prone balance of power, nor flow from a new Bretton Woods-San Francisco as in 1944–1945 but from an intensification and expansion of G20 governance that will generate and coordinate more comprehensive, stronger multilateral organizations for the benefit of all.*

**Key words:** international institutions; global governance; COVID-19 crisis; IMF; World Bank; WTO; WHO; EU; BRICS; G7; G20

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## Introduction

It is difficult to assess the impact of COVID-19 on global governance, international institutions and international relations. However, now is the time to start reflecting on three questions as a guide to shaping better answers and outcomes for the post-COVID-crisis world. First, were the actions undertaken by international institutions adequate, coordinated and timely? Second, could the outbreak have been contained if the global governance system had not been in a state of severe

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<sup>1</sup> The article was written on the basis of the RANEPA state assignment research programme.

strain, with many of the gaps exposed and reforms promised in the wake of the 2009 financial and economic crisis unfulfilled, its key causes unaddressed, and unilateralism rising among its key members? In addition, was the COVID-19 crisis exacerbated by the crisis of multilateralism? Third, and most difficult, what is the future of global governance after the COVID-19 crisis?

Three months into the crisis, three answers emerged. First, there has been inadequate action to produce a timely, coordinated international response from all of the major multilateral organizations and from the newer plurilateral summit institutions of the BRICS group of Brazil, Russia, India, China and South Africa, the Group of 7 (G7) and the Group of 20 (G20). Second, the failure of these global governance institutions was due not only to the severe strains caused by leading members' unilateralism and competition but also to their very architecture, designed in 1945 and poorly matching the needs of today's intensely globalized world. Third, global governance in the post-COVID world will not descend into the old war-prone balance of power, nor flow from a Bretton Woods-type arrangement as in 1944–45; rather, an intensification and expansion of G20 governance will generate and coordinate more comprehensive, stronger multilateral organizations for the benefit of all.

## Inadequate Actions

The coordinated international response thus far has often been assessed as late and inadequate. Indeed, the first case of a pneumonia of unknown cause was reported to the World Health Organization (WHO) Country Office in China on 31 December 2019. One month later, on 30 January 2020, the WHO declared a public health emergency of international concern (PHEIC) [WHO, 2020a]. It promptly released a strategic preparedness and response plan to support the national and international authorities in developing context-specific national and regional operational plans [Ibid., 2020b]. The plan called for a total resource requirement of \$675 million, of which \$61.5 million was for the WHO's urgent preparedness and response activities from February to April 2020. By 29 February, 85,403 cases were confirmed globally, with 6,009 in 53 countries outside of China [Ibid., 2020c]. COVID-19 was rapidly spreading in Europe, which was struggling to contain the outbreak [Beaumont, 2020]. In the face of COVID's swift assault, the lack of concerted global action by the major multilateral organizations stood out [Grimalda, 2020].

## Global Financial Institutions

Only on 3 March 2020 did the International Monetary Fund (IMF) and the World Bank Group (WBG) make their first explicit statement that they stood ready to use all available instruments to confront the crisis and its severe economic and financial effects [IMF, 2020]. The following day the International Monetary and Financial Committee endorsed the IMF's actions. The IMF made available \$50 billion through the rapid-disbursing emergency financing facilities for low-income and emerging-market countries. Of this, \$10 billion was available at a zero interest rate for the poorest members through the Rapid Credit Facility. At the G20 leaders' summit on 26 March, IMF Managing Director Kristalina Georgieva announced that the IMF, with the WBG and other international organizations had a combined financial capacity of \$1 trillion for emergency financing. She asked for G20 leaders' support to double it and boost global liquidity through a sizeable special drawing right allocation and by expanding the use of swap-type facilities at the Fund. On 26 March the IMF executive board approved a reform of the Catastrophe Containment and Relief Trust (CCRT). By the end of March almost 80 member countries sought access to rapidly disbursing, low-conditionality IMF emergency facilities to meet the immediate pressures arising from the COVID-19 crisis [Thomsen, 2020].

Simultaneously the World Bank and International Finance Corporation's (IFC) boards of directors approved an increased \$14 billion package of fast-track financing to assist companies and countries to prevent, detect, and respond to the rapid spread of COVID-19. By the end of March projects were being finalized in 60 countries for up to \$2.8 billion [Malpass, 2020].

## Global Health Governance and the World Health Organization

As the central multilateral organization for health, the WHO, founded in 1948, was slow to act. On 31 December the WHO had been alerted to a potential novel virus by Chinese authorities, described in patients with “pneumonia-like” symptoms. On 22–23 January, its director-general convened an emergency teleconference under the International Health Regulations (IHR) to discuss whether to declare the outbreak a PHEIC [WHO, 2020d]. By that time, cases had been confirmed outside of China, in Korea, Japan, Thailand and Singapore. The Emergency Committee members expressed “divergent views” and advised the WHO “to consider a more nuanced system.” As cases rose and spread throughout Asia to Australia, Europe and North America, on 28 January the WHO said it would send its team to China to support efforts to contain the outbreak there [Rabin, 2020]. On 30 January, the Emergency Committee convened for a second time and declared COVID-19 a PHEIC [WHO, 2020a]. The Committee recommended the rapid deployment of and access to potential vaccines but against implementation of travel restrictions.

On 5 February, the WHO issued a strategic preparedness and response plan for the period between February to April, called for \$675 million for its implementation [Ibid., 2020e, 2020f], and announced it would convene a global research and innovation forum on 11–12 February. On 8 February, the WHO assembled a team of experts, which landed in China on 9 February [Allyn, 2020; Ghebreyesus, 2020a; Nebhay, 2020]. On 10 February, Donald Trump, president of the United States – the WHO's largest donor – slashed the U.S. contribution by 50% in his budget proposal [Hansler, 2020; WHO, n. d., a]. On 15 February, at the Munich Security Conference, the WHO's director-general warned that COVID-19 had “pandemic potential” that would require an “immediate and large-scale response” [WHO, 2020g]. On 16 February, another WHO-led team of experts landed in China, now on a joint mission with China [Ghebreyesus, 2020b]. More WHO experts landed in China on 22 February [Jaipragas, Zheng, 2020]. On 25 February a joint WHO-European Centre for Disease Prevention and Control arrived in Rome [WHO, 2020h]. On 25 February, the WHO announced there were more new COVID-19 cases outside China than within it [Kiernan, Socrates Bardi, 2020]. On 26 February, the WHO director-general, in his opening remarks to the joint WHO-China collaboration mission briefing, stated that continued vigilance was needed and that using the word “pandemic” brought risks of “amplifying... fear and stigma” and “paralyzing systems.”

On 11 March the WHO declared COVID-19 to be a pandemic [WHO, 2020i]. On 13 March, it said Europe was the new epicentre of the outbreak [Schnirring, 2020].

## Regional Responses

Similarly late and lacking were regional organizations, led by the most powerful European Union. The EU Extraordinary Health Council convened on 13 February and called on EU members to act together to increase preparedness and activate existing funding mechanisms to support members' preparedness [Council of the European Union, 2020a]. But it took several weeks, many more casualties and the Croatian presidency's decisive consistent push, including the full activation of the Integrated Political Crisis Response (IPCR) arrangements, to coor-

dinate and enable the needed action. The Eurogroup agreed on an economic policy response on 10 March [Council of the European Union, 2020b]. It launched the Coronavirus Response Investment Initiative package consisting of €37 billion in public investments to mitigate the impact of the crisis, and to save lives, jobs and businesses it also offered flexibility in applying the Stability and Growth Pact rules and extended the EU Solidarity Fund's scope [EC, 2020a]. The initiative was considered far from adequate. Thus, the EU Council followed up with additional measures allowing flexibility and transfers in mobilizing the European Structural and Investment Funds. An additional €3 billion was mobilized from the EU's budget to directly support the healthcare systems of its members [Ibid., 2020b]. Nevertheless, the initial delay, national egoism in the struggle for medical goods, responsibility shifting, and an "only-for-me" response left a long shadow over the EU's spirit of solidarity, even as its members' death tolls relentlessly rose.

## Trade and Global Value Chains

In coping with the consequent trade crisis, the World Trade Organization (WTO) has struggled too. By some estimates, the negative impact of COVID-19 on global value chains, international trade, and investment may be much worse than that from the global financial crisis of 2008–09 [UNCTAD, 2020]. The WTO's goods and services trade barometers registered continued weakening of world trade in both components [WTO, 2020]. Further declines are expected. The disruptions result from the lockdown measures that states have taken to protect their citizens, but also from trade restrictions and bans on medical and health-related goods. While WTO rules allow members to adopt trade measures necessary to protect public health and public welfare, these measures should be communicated to the WTO, applied in a manner that does not discriminate between WTO members, and not constitute disguised restrictions on international trade. Only a handful of notifications regarding these COVID 19-related trade measures have been received by the WTO [Ibid., n. d.]. The WTO can do little else but monitor any measures to restrict or facilitate trade imposed by WTO members and, in partnership with the United Nations Conference on Trade and Development (UNCTAD) and other institutions, assess the potential impact on global economic growth and development, alert member governments of the consequences, and call on them to minimize and notify restrictions.

## The BRICS

The plurilateral summit institution of BRICS, like that of the G7 and G20, has the architectural advantage of being delivered directly at the leaders' level, with all the authority and comprehensive coverage that they alone command. These institutions have mandates that embrace and integrate the key issues of health, the economy, development and trade, and much more. They have thus moved to compensate for inadequacies of the major multilateral organizations, although not as actively as their unique architecture allows.

BRICS has had health as a priority with an institutionalized foundation. It has a good track record of commitment and compliance dating back to the 2012 Delhi summit. However, BRICS did not come up with a statement of collective response nor hold an emergency summit in face-to-face or virtual form.

The BRICS members did express their solidarity with China, where the COVID-19 pandemic began, and their commitment to work together. At their first meeting on 11 February 2020, the leaders' personal representatives, or "sherpas," underlined the importance of avoiding discrimination, stigma and overreaction while responding to the outbreak [BRICS Russia,

2020]. The call was timely in view of the Trump administration's attempt to drive xenophobic sentiment toward China and blame the spread of corona virus on China [Cillizza, 2020]. On 19 March the New Development Bank board approved a RMB 7 billion loan (about \$1 billion) under its Emergency Assistance Program in Combating COVID-19 for China [NDB, n. d.].

The issue and possible coordinated actions are being discussed. However, a new breakthrough initiative is unlikely for two reasons. First, the BRICS states already have a long-standing commitment to work together to manage risks related to emerging infections with pandemic potential and to contribute to ongoing efforts to strengthen health sectors, including through the WHO and other international organizations. Second, BRICS supports and is committed to cooperation with the WHO. Thus it is likely that BRICS will build on existing commitments and contribute to the WHO's key initiatives to combat the spread of the virus, including the COVID-19 Strategic Preparedness and Response Plan [WHO, 2020b], the Country Preparedness and Response Status Assessment [Ibid., 2020j] and the COVID-19 Solidarity Response Fund [WHO, United Nations Foundations, Swiss Philanthropy Foundation, n. d.<sup>2</sup>]. With regard to the economic impact of the outbreak, BRICS will continue to try to coordinate the policy response in the G20.

## The G7

The major market democracies constituting the G7 held an emergency virtual summit on 16 March, following emergency meetings of their health ministers on 3 February and their finance ministers and central bank governors on 3 March. At the virtual summit the G7 leaders produced 31 commitments, led by those on health. They committed to act together to resolve the health and economic risks caused by the COVID-19 pandemic and to set the stage for a strong recovery, sustainable economic growth and prosperity [G7, 2020; Kirton, 2020a]. They pledged support for the WHO. But there was no promise of additional, urgently needed money for the WHO, either on a one-time emergency basis or permanently, to put in place the global health infrastructure to control COVID-19 and pandemics still to come [Kirton, 2020b]. The G7 tasked the finance ministers to work closely with the IMF, the WBG and other international organizations to design and implement international financial assistance to help countries facing the health and economic shock of COVID-19. However, they did not make a joint plan or concrete commitments to address the economic recession, international trade disruptions, or unemployment risks. Yet they did tell their health and finance ministers to meet weekly to follow up, promised to meet themselves very soon, and called upon the G20 to support and amplify its efforts.

## The G20

This the G20 did. The first G20 statement came on 6 March from the ministers of finance and central bankers. It was followed by the sherpas' statement on 12 March and a virtual meeting by the ministers of finance and central bankers on 23 March to prepare for the G20 leaders' extraordinary summit, convened by the Saudi G20 Presidency, on 26 March. The 47 commitments made by the G20 leaders affirmed the G20's first distinctive foundational mission promote financial stability, but also gave attention to the G20's second mission to make globalization work for all. First, the G20 pledged to do whatever it took to overcome the pandemic, along with the WHO, the IMF, the WBG, the United Nations (UN), and other international

<sup>2</sup> As of 18 March 2020, the Fund raised around \$153.5 million. China, the only BRICS country to contribute, donated \$20 million to the Fund [WHO, n. d., b].

organizations. They promised to ensure adequate financing to contain the pandemic and protect people; strengthen the WHO's mandate in coordinating the international fight against the pandemic; provide immediate resources to the WHO's COVID-19 Solidarity Response Fund and strengthen health systems globally, including through supporting the full implementation of the WHO's International Health Regulations (IHR, 2005).

Second, the G20 committed to inject over \$5 trillion into the global economy and use all available policy tools, including large-scale fiscal support, to minimize the economic and social damage from the pandemic, restore global growth, maintain market stability, and strengthen resilience. Third, the leaders reiterated the goal to realize a free, fair, non-discriminatory, transparent, predictable and stable trade and investment environment, and to keep the markets open; they further pledged to continue working together to facilitate international trade and coordinate responses in ways that avoid unnecessary interference with international traffic and trade.

Fourth, the G20 confirmed its commitment to restore global economic stability and lay out solid foundations for strong, sustainable, balanced and inclusive growth. Fifth, the leaders asked the finance ministers and central bank governors to coordinate on a regular basis to develop a G20 action plan in response to COVID-19 and to work closely with international organizations to swiftly deliver the appropriate international financial assistance.

By its concrete and time-bound commitments the statement was somewhat reminiscent of the G20 Washington summit final document. It raised hopes that the G20 would fulfil its potential as the premier forum for global economic governance and harness its political leadership to address the crisis. The G20 finance ministers and central bank governors promptly acted on the leaders' request to develop the joint G20 Action Plan, which was delivered by mid-April.

## The UN

The UN was the slowest to respond in a material or institutional way. It launched a COVID-19 Global Humanitarian Response Plan [UN, 2020a] on 25 March. This was a \$2 billion appeal to fight coronavirus in the most vulnerable countries. UN Secretary-General António Guterres called on everyone to act together to address the impact and lessen the blow to people [Ibid., 2020b].

The UN Security Council, which during the Ebola outbreak in Africa in 2014 had produced a resolution, was unable to do so now due to disagreements between two of its permanent five veto powers, the United States and China. The Security Council did not meet at the UN headquarters for three weeks as all of its members self-isolated at home.

The first UN General Assembly (UNGA) resolution on the outbreak calling for international cooperation was adopted on 2 April after consideration of two different drafts under a so-called "silence procedure." By that date almost 900,000 confirmed cases and 45,424 deaths had been registered in 207 countries.

UNGA Resolution 74/270, sponsored by Ghana, Indonesia, Liechtenstein, Norway, Singapore and Switzerland, recognized that the pandemic required a global response based on unity, solidarity, and renewed multilateral cooperation [Ibid., 2020c]. However, it did not contain a pledge to ensure that national protective measures were effective while minimizing the negative effect on people, other states, trade and the global economy; nor did it contain a commitment to refrain from raising trade barriers, imposing new export restrictions or implementing protectionist and discriminatory measures inconsistent with the WTO rules [Ibid., 2020d, Draft Para. 6 and 7]. The Declaration of Solidarity was the lowest common denominator. It came too late, with very little substance or promise of collective action.

Secretary-General Guterres declared COVID-19 to be the most challenging crisis since the UN's founding in 1945. Yet his call for a ceasefire in all global conflicts so countries could

concentrate on combating the health crisis went unheeded in Syria, Yemen, Libya, Afghanistan, Mali and Columbia, while North Korea launched four missile tests in the month before 5 April. By this time, COVID-19 had infected over one million people and killed over 54,000 in 180 countries and territories.

A deeper UN failure was the refusal of its members to provide funds as they were legally obliged to do. By early April the UN faced a serious liquidity crisis as members paid less of their assessed dues for 2020 than usual, even as U.S. costs to confront the COVID crisis rose. Before the COVID-19 crisis, regular budget contributions had arrears of \$771 million at the end of 2019, a 34% increase from the previous year and the highest in a decade. As members used their scarce funds to respond to the crisis, UN contributions dropped sharply in the first quarter of 2020, producing a collection gap of over \$220 million and a hiring freeze. The UN had only \$1.4 billion for its peacekeeping operations, too little to pay the countries contributing troops and police for the March and June quarters. Guterres thus had to launch appeals for two special funds, one for \$2 billion to help COVID-afflicted countries a second one of \$8–9 trillion, or 10% of global gross domestic product, to combat the pandemic.

## Preliminary Conclusions

Coordinated collective action by all of the key international institutions was late and insufficient. A key reason for this is that political fragmentation and tensions prevailed in international politics. International institutions entered a phase of weakening, due partly to American withdrawal, partly to discord among major powers, and partly to the unprecedented comprehensive, interconnected speed and scale of the crisis [Duclos, 2020]. A second reason is “irresponsible wishful thinking by political leaders and the obstinate dominance of a nationalistic approach to global problem-solving” [Grimalda, 2020]. A third is that there is no premier forum for global cooperation for the well-being and protection of people. Although established for this mission, the UN fell victim of the crisis in multilateralism and an organizational architecture that may have made sense in 1945 but does not in today’s intensely globalized world. The G20 is much better at coordinating actions on its first foundational mission, to promote financial stability and generate strong, sustainable and inclusive growth, than it is on its second mission to make globalization work for all. Besides “this devastating disease struck the world when the G20 nations’ instinct for multilateralism and global cooperation had weakened; when U.S. – China recriminations were running high on a range of issues, including the name and origin of the disease and ascribing responsibility for its spread; and when the badly under-resourced World Health Organization (WHO) was under fire for its inordinately slow response and unjustifiably delayed declaration of the Coronavirus Disease (COVID-19) as a pandemic” [Bhatia, 2020].

It took time and effort for G20 leaders to come together to forge a more ambitious and comprehensive collective response to the COVID-19 crisis and its economic and social impacts. The leaders’ statement of 26 March was criticized for failing to provide guidance on the economic challenges posed by the health crisis, to endorse a fresh allocation of the IMF’s special drawing rights, to increase the permanent base budget of the WHO, or to make a collective pledge to address the root causes of the pandemic and invest in health-security preparedness, addressing a gap that long predates the current crisis [Goodman, Segal, Sobel, 2020].

However, the G20 did commit to mobilize new money for health, economic growth, jobs, and development, and tasked their health and finance ministers to develop a set of G20 urgent actions on jointly combatting the pandemic by April 2020. The also pledged to work swiftly and decisively with the WHO, the IMF, the WBG, and multilateral and regional development banks to deploy a robust, coherent, coordinated, and rapid financial package and to address

any gaps in their toolkit. But a much more decisive and ambitious set of actions was expected. The G20 should deliver quickly on the pledges. By the next meeting they promised to convene as the situation required, which it certainly does now, and that the G20 should forge concrete commitments “to protect human life, restore global economic stability, and lay out solid foundations for strong, sustainable, balanced and inclusive growth” [G20, 2020]. There is no other global leader to take responsibility for safeguarding peoples’ safety, health and well-being. The G20 must fulfil its potential as the world’s premier economic forum and its mission to make globalization work for all people. “Out of this crisis must come not only the reforms to the international architecture left on the table in 2009 but new levels of co-operation that will deliver a quantum leap: a commitment to deliver the global public goods urgently needed by a world beginning to understand that it is both far more interdependent and far more fragile than ever” [The Office of Gordon and Sarah Brown, 2020].

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# Globalization's Implications for G20 Governance<sup>1</sup>

J. Kirton

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## Abstract

*The rapid globalization of money, goods, services, taxation, knowledge, people, political ideas, digitalization, and especially pathogens and ecological pollutants has intensified, along with rising inequality, multipolarity, protectionism, isolationism and geopolitical tensions. Together these factors present new challenges to 21st century global governance led by the systemically significant states which make up the Group of Twenty (G20). G20 governance has expanded in response, but with more success on its old, incompletely globalized economic agenda than on its newer, more globalized digitalization, health pandemics and climate change agendas. The most recent G20 summit in Osaka, Japan on 28–29 June 2019 did make advances on tax and digitalization but not on the looming health risks and the existential threat of climate change. Preparations for the Saudi Arabian-hosted Riyadh summit, to be held on 21–22 November 2020, have made some progress on the latter amidst the unprecedented crisis posed by the COVID-19 pandemic. The crisis shows that the G20's architecture needs to be further strengthened by institutionalizing G20 environment and health ministers' meetings; inviting the executive heads of the United Nations (UN) bodies for climate change, biodiversity, the environment and health, as well as the leaders of key outside countries, to the summits; giving the UN and World Health Organization the same G20 status as the International Monetary Fund and World Bank; and holding a second annual summit at the UN each September focused on the sustainable development goals.*

**Key words:** G20; globalization; digitalization; climate change; Sustainable Development Goals

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## Introduction

### ***The Challenge***

The rapid globalization of goods, services, taxation, knowledge, people, digital technology, and above all pathogens and ecological pollutants, along with rising inequality and multipolarity, presents new challenges to 21st century global governance by the systemically significant states which make up the Group of Twenty (G20). Such changes have intensified protectionism, isolationism and geopolitical tensions. They have rapidly made climate change, biodiversity loss and health threats such as the current COVID-19 pandemic the greatest threats

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to strong, sustained, balanced, inclusive economic growth and to the G20's distinctive foundational missions of promoting financial stability and making globalization work for all [Kirtan, Kokotsis, 2015].

### ***The Debate***

These dynamics have inspired a debate among several schools of thought about the dynamics of contemporary globalization and the effectiveness of the G20 in response.

The first school sees G20 failure. Martin Gilman [2018, p. 9] claims that “deglobalization has become a factor in the internal politics of too many countries” and that its source in the economic dynamics and policy “in some of the major G20 economies cannot be sustained much longer.” He writes that “the concerted, post-crisis efforts of the G7 [Group of Seven major market democracies], abetted by the G20, to restore the prevailing liberal global economic framework have been misguided.” He adds that “the G20, especially at the summit level, has become an anachronistic photo op” [Ibid., p. 10]. He concludes that “ironically the forces of deglobalization are intensifying almost despite the global reach of the internet — as seen in areas from security, migration, taxation and trade” [Ibid., p. 12]. He locates the cause in a declining, disruptive United States under President Donald Trump, the decline of G7 economies, and the rapid rise of the emerging G20 economies.

The second school sees G20 decline. Harold James [2017] writes: “Each major challenge — the 1970s inflation and oil price shocks and the recent global crisis — produced some new approaches to multilateral cooperation and coordination: the G5 in 1975 and the G20 advanced and emerging market economies in 2008. In each case, however, a productive initial meeting was followed by a process of routinization that sapped the urgency and capacity to generate major breakthroughs and policy improvements.” He points to Big Data and transparency as a solution. Jean Pisani-Ferry [2019, p. 2] similarly states that “the elevation of the G20 to leaders’ level adjusted the political leadership to the new reality of the global economy... but international macroeconomic coordination was short lived.” A variant sees a role for the G20 in confronting the COVID-19 crisis, but only if its most powerful states cooperate and it adds a G4 inner steering group of the United States, China, Germany and France [Stephens, 2020]. Thus, due to U.S. — China disagreements, the G20 produced only limited results at its emergency summit on 26 March 2020 [Goodman, Segal, Sobel, 2020].

The third school sees G20 economic success and ecological failure. Stephen Bernstein [2019, p. 18] see the G20 effectively responding to the 2008 global financial crisis in international financial institutional reform, development and trade with their environmental failures, but not on environmental issues. They see the G20 doing better than either the G7 or the BRICS grouping of Brazil, Russia, India, China and South Africa in this regard. They conclude “that much more serious repercussions for the international order follow failures of economic leadership and responsibility than follow failures of environmental leadership or great power responsibility.” In a similar spirit, Michael Motala [2019a] concludes that the G20 and the Organisation for Economic Co-operation and Development (OECD) have been a partial success on tax, with their achievements on first order compliance not extending to enforcement.

The fourth school sees continuing G7 success in governing globalization, even with the advent of the more inclusive G20 in response to the global financial crises of 1997 and 2008 [Oldani, Wouters, Andrione-Moylan, 2019, p. 5]. However, both the G7 and G20 struggle to cope with the upsurge in antiglobalization populism in many of their most powerful members. Others see similar potential for the G20 to induce the United States, China and others to cooperate in response to the proliferating COVID-19 shock [Albright et al., 2020; Nye, 2020].

The fifth school sees increasing G20 success on digitalization. John Kirton and Brittaney Warren [2018] see G20 digitalization governance expanding in breadth and depth beyond its 2008 framework, moving from crisis response to crisis prevention. This success was fuelled partly by “the shocking surge in populism bred by inequality in the UK and U.S. in 2015 and 2016, by the failure of the established multilateral organizations in response, by the global predominance and equalizing capabilities of G20 members in specialized digital capabilities and their convergence in the economic growth through openness that digitalization brought” [Ibid., p. 16]. However, the G20’s hosting by China in 2016 and Germany in 2017 were the primary causes of success.

### ***Puzzles***

Although each of these schools offers valuable insights, all omit a comprehensive, systematic analysis of the dynamics of globalization in the major processes through which it unfolds. Nor do they focus on how each of the major global governance institutions, led by the G20, recognize and frame the process of “globalization,” its causes and its consequences, and how, why, and how well they respond. Moreover, the focus remains on the old pioneering globalization processes of finance and trade rather than shifting to processes of digitalization, health, and climate change in which globalization is more advanced and where the opportunities and threats are more extreme. This study makes a distinctive contribution to the literature by filling these important gaps.

### ***Thesis***

This study argues that the rapid globalization of money, goods, services, taxation, knowledge, ideas, people, digital technology and above all pathogens and ecological pollutants – combined with rising inequality, multipolarity, protectionism, isolationism and geopolitical tensions – presents new challenges to 21st century global governance. G20 governance has expanded in response, but has had more success with its old, incompletely globalized economic agenda than on its newer, more fully globalized digitalization, health, and climate change agendas. The G20 summit in Osaka, Japan on 28–29 June 2019 made advances on tax and digitalization, yet failed to cope with the major health risks and the existential threat of climate change. Preparations for the Saudi Arabian-hosted summit to be held in Riyadh on 21–22 November 2020 have been more promising, especially as the United Nations (UN)-based process of delivering the sustainable development goals (SDGs) intensifies and after the COVID-19 crisis struck (see [Kirton, 2019b]). Yet the crisis shows that G20 architecture needs to be further strengthened by institutionalizing the new G20 environment ministers’ meeting; inviting the executive heads of the UN bodies for health, climate change, biodiversity, the environment and health, as well as the leaders of countries most vulnerable and most rapidly becoming carbon neutral to the summits; giving the UN secretary-general and director-general of the World Health Organization (WHO) the same G20 status as the heads of the International Monetary Fund (IMF) and World Bank; and holding a second annual summit at the UN each September, focused on the SDGs.

To support this thesis, this study examines in turn the dynamics of 21st century globalization, G20 summit performance in key aspects of globalization, its performance at the Osaka summit in July 2019, preparations and prospects for the Riyadh summit in November 2020, and the potential to strengthen governance through five institutional reforms.

## Globalization in the 21st Century

The creation of the G20 at the level of finance ministers and central bank governors was spurred by the demand for a new form of global governance, driven by the latest stage of globalization in the form of the Asian-turned-global financial crisis from 1997 to 1999 [Kirton, 2013]. It arose in the familiar field of finance, but two decades later acquired the new central dimension of climate change. Here globalization became geographically complete, fully inclusive, far more harmful than helpful, and extremely difficult to control or reverse, even with the increasing action taken by the G20 summit from 2008 to 2020 [Kirton, Kokotsis, 2015; Kirton, Kokotsis, Warren, 2019].

### ***Globalization's Growing Demand for Global Governance***

Among scholars there has been great debate about when globalization began, what forms it has taken, what its course and consequences have been and how the concept is best conceived [Sassen, 2007; Scholte, 2005; Sen, 1999; Stiglitz, 2002; Woods, 2006]. In the current era of mass, multidimensional globalization, people have become more directly globally connected through language, information, communication, transportation and technology, the internet and mobile phones, terrorist attacks, global financial crises, health pathogens, biodiversity loss, ocean pollution, and climate change. This was fuelled by the massive opening and democratization of many states and societies brought by the Cold War victory in 1989, much of which remains intact.

Contemporary globalization consists of the unprecedented, step-level increases in the speed, scope, scale, inexpensiveness, global reach, contributing actors, and domestic intrusiveness of natural and socially driven transborder flows of information, images, individuals, money, goods, technology, disease, and pollutants. This creates a single global society that national governments acting alone cannot control. This intensely increasing interconnectedness produces the death of distance, the death of delay, and the death of discreteness, but not the death of difference, as shown by the current protectionist, populist and nativist blowback in leading countries [Kirton, 2019a].

Globalization can be measured by how many people are instantly and directly involved in it as contributing actors or as subjects experiencing its consequences. By this measure, its pace and level have varied widely across its many component parts.

In finance, the 2008 American-turned-global financial crisis was much stronger on all dimensions than its 1997–99 predecessor had been. Yet many people remain uninvolved in finance, even in the most basic sense of having a bank account, let alone a mortgage.

In the related economic fields of trade and investment, the same is true. Moreover, in the first seven months of 2019 world trade declined, with exports down in July by 0.4%, according to the Netherlands Bureau for Economic Policy Analysis [Romel, 2019]. In tax, only a minority of the world's people are now directly engaged in international taxation, tax avoidance or tax evasion, or have been directly affected by those who engage in these activities.

In digitalization, by 2018, 90% of people lived within range of at least a 3G mobile network, but many could not afford to use it [United Nations, 2019, p. 12]. The digital divide remained, as over 80% of individuals in developed countries were online, but only 45% in developing countries and only 20% in the least-developed ones. By 2019, five billion smartphones were being used globally and over half of the world's population was connected to the internet in some form. However, not everyone could freely communicate through the national firewalls or shutdowns that some countries imposed.

In health, people have become more interconnected due to the global spread of non-communicable disease, emerging threats such as antimicrobial resistance, and the periodic eruption of acute outbreak events, notably severe acute respiratory syndrome (SARS) in 2003, the Middle East respiratory syndrome and Ebola in 2014, and the latter again in 2019. The current COVID-19 pandemic was a step-level jump. By 7 April 2020, four months after it started in China in December 2019, it had infected 1,381,014 people and caused at least 78,269 reported deaths in over 200 countries and territories, bringing feature and behavioural changes with it.

Unlike the 1918–19 influenza pandemic, the COVID-19 pandemic rapidly became an economic, trade, financial, employment, social, political, and security crisis. By early April, the world had plunged into a severe recession, international trade was cut, and the International Labour Organization (ILO) had estimated that 195 million jobs would be lost globally [Strauss, 2020]. The pandemic helped Hungary turn from democracy to authoritarianism, reduced the military capacity of the U.S. and others, and increased tensions between the United States and China.

Moreover, the COVID-19 crisis showed how the world's most capably country could quickly become the most vulnerable one, due to the intense interconnectivity created by globalization. By early April, the United States led the world in the number of recorded COVID-19 cases and soon after would also lead in recorded deaths. It was the states of the G7 and G20 that were the most vulnerable; the global death toll on 6 April was led by Italy with 17,127, the United States with 12,854, France with 10,328 and the United Kingdom with 6,159, followed by China with 3,333, Germany with 2,016, Turkey with 725, Brazil with 688, and Canada with 381. All G7 members but Japan were in the top 10 in terms of the global death toll, all G20 members had recorded deaths, and G20 members along with Iran led the world's death toll.

In the less visible, cumulative dimension of climate change, and the closely related fields of biodiversity and oceans, globalization is complete. Compounding catastrophic consequences make climate change the greatest financial and economic threat of the current and coming decades. A report released by the Intergovernmental Panel on Climate Change (IPCC) on 8 October 2018 noted that the world would suffer \$54 trillion in economic damages due to global warming of 1.5°C between now and 2040 [Hoegh-Guldberg et al., 2018; Keefe, 2018]. Between 1998 and 2017, direct economic damages from disasters totalled almost \$3 trillion, with climate-related disasters accounting for 77% and rising by 151% [UN, 2019, p. 23]. Global investors estimated that climate change could cause permanent economic damage of up to four times that of the 2008 global financial crisis, with one member estimating that a 4°C temperature rise beyond pre-industrial levels could cause \$23 trillion in global economic losses by 2100 [Nace, 2018]. Hans Helbekkmo of McKinsey added that “we could see loss rates [from mortgage defaults] similar to the 2007 [subprime crisis] in the next 10 to 20 years” (quoted in [Tett, 2019]). Climate change is also associated with health risks such as antimicrobial resistance and COVID-19 as it helps concentrate animals in closed spaces close to humans, transmitting pathogens from animals to humans who have no natural resistance to them, nor treatments or vaccines.

Contemporary globalization requires G20 governance. The transnational spread of natural, social and economic forces requires governments to engage in greater international cooperation as protective national measures largely fail. Among the many candidates, the G20 stands as the institution most likely to govern globalization effectively. This is due to its 21<sup>st</sup> century design as a group of systemically significant states commanding not only globally predominant relative capability in almost all relevant spheres, but also to the intense connectivity and resulting mutual vulnerability that renders them all effectively equal in their need to cooperate to save themselves and the global community as a whole [Kirton, 2013].

## G20 Summit Performance in Globalization's Key Sectors

From its start in 2008 through to 2019, the G20 summit governed the leading sectors of contemporary globalization with varying degrees of effectiveness (see Appendix A).

The concept of globalization was first introduced into global summit governance at the 1988 G7 summit in Toronto [Kirton, 2013]. In 1999 the first official G20 statement quoted Canadian finance minister and G20 chair Paul Martin as saying "The G20's work will focus on translating the benefits of globalization into higher incomes and better opportunities for people everywhere... There is virtually no major aspect of the global economy or international financial system that will be outside the group's purview" [G20, 1999a]. The communiqué of the first meeting of G20 finance ministers and central bank governors, held in Berlin on 15–16 December 1999, similarly stated: "They discussed a range of possible domestic policy responses to the challenges of globalization, and... the role of the international community in helping to reduce vulnerability in crisis" [Ibid., 1999b]. At their second meeting, held in Montreal on 25 October 2000, their communiqué focused fully on globalization and added to its trade and finance components tax evasion, money laundering, corruption and "serious issues such as infectious disease, agricultural research and the environment" [Ibid., 2000].

While G20 summitry began in 2008, leaders have recognized the process of globalization in their outcome documents at only three of the 14 summits they have held to 2019.

At their second summit, in London in April 2009, G20 leaders [2009] stated: "We believe that the only sure foundation for sustainable globalisation and rising prosperity for all is an open world economy based on market principles, effective regulation and strong global institutions." They agreed to reform "our international financial institutions for the new challenges of globalisation." In contrast to the post-1945 compromise of embedded liberalism (see [Ruggie, 1983]), social protection from international openness was now to come from international regulatory institutions, rather than domestic redistributive ones.

However, when the G20 next addressed globalization at Cannes in November 2011, the leaders returned to the traditional 1945 formula. They stated: "We are determined to strengthen the social dimensions of globalisation. Social and employment issues, alongside economic, monetary and financial issues, will remain an integral part of the G20 agenda" [G20, 2011].

This return to the traditional embedded liberalism acquired new components when the G20 [2017] next addressed globalization, at the Hamburg summit in July 2017. Its declaration said: "Globalisation and technological change have contributed significantly to driving economic growth and raising living standards across the globe. However, globalisation has created challenges and its benefits have not been shared widely enough. By bringing together developed and emerging market economies, the G20 is determined to shape globalisation to benefit all people." To do so the leaders pledged to "exchange experiences on... technological change, and on appropriate domestic policies." To achieve "an inclusive, fair and sustainable globalisation" they committed to "fostering the implementation of labour, social and environmental standards and human rights." They identified as the driving forces "the impact of new technologies, demographic transition, globalisation and changing working relationships on labour markets." They thus added digitalization and the natural environment to their globalization problématique.

In general, G20 summit performance was high among the core economic subjects (macroeconomic policy, financial regulation, tax) on which the G20 summit first focused, but not on trade where globalization remained relatively low. G20 performance was lower in the newer fields of health, digitalization, climate change and energy, where globalization was relatively high. The G20 has thus been an effective governor of the old economic globalization in re-

sponse to the shocks that globalization has brought, but has been less effective in proactively governing the new globalization, or the acute shocks that have proliferated in recent years. A systematic examination of G20 summit performance by the established methodology supports this claim [Kirton, 2013; Kirton, Kokotsis, 2015; Global Governance Program, 2019a; 2019b].

On the core economic subject of macroeconomic policy from 2008 to 2019, 467 commitments were made at G20 summits, constituting 19% of the 2,526 commitments made. This put macroeconomic policy in first place. Compliance averaged a high 80%, well above the 71% compliance average overall [Wang, 2019]. The closely related field of financial regulation had 340 commitments (13% of the total) and compliance of 80% [Nikolaeva, 2019]. Tax received 85 commitments (3.5% of the total) and compliance averaged a very high 85% [Motala, 2019a; 2019b]. Trade received 169 commitments (7% of the total) and had compliance only 67% [Marchyshyn, 2019].

Digitalization had 28 core commitments and 37 related ones, for a total of 65. Compliance with the five core commitments assessed averaged a very low 57%. However, the four digitally related development commitments assessed averaged a high 85% [Williams, 2019]. Health had 75 commitments with 73% compliance [Warren, 2019b] (see Appendix B). Climate change had 92 commitments with 69% compliance [Ibid., 2019a] (see Appendix C). The closely related field of energy had 155 commitments with 71% compliance [Kokotsis, 2019].

Thus, the core subjects of the old, partial economic globalization tended to have high G20 performance and those of the newer, more complete digital, health, and ecological globalization had low G20 performance.

## G20 Governance at the Osaka Summit in 2019

This pattern was evident at Osaka in June 2019, where G20 leaders performed well on their priorities of tax and digitalization, did less well on health, and failed on the urgent, existential threat of climate change.

### **Tax**

On the old issue of tax the G20 excelled in partnership with the OECD. At Osaka, G20 leaders agreed to produce by 2020 a revolutionary regime to ensure that companies paid their fair share of taxes in the countries where the value was created by their customers and users, rather than in the country where they arbitrarily declared their headquarters to be. The historic formula based on static, exclusive, sovereign territorial states that had prevailed since 1648 would be replaced by one appropriate for the 21st century world of globalized flows. The new regime could be accompanied by a minimum tax on firms to ensure they could not hide in tax havens. The new regime, once implemented, will do much to help the governments poor and rich countries alike to raise the financial resources required to meet their people's needs.

### **Digitalization**

The G20's greatest achievement was the launch of the Osaka Track for "data free flow with trust," Japanese prime minister Shinzo Abe's signature initiative as host of the summit. Almost all G20 leaders, including U.S. president Donald Trump and Chinese president Xi Jinping, agreed to launch this process for rules-based multilateral trade liberation by providing a highest-level political push to the e-commerce negotiations at the World Trade Organization (WTO), aiming for substantial progress by June 2020. Although India, South Africa and Indo-

nesia did not join, Indian prime minister Narendra Modi privately assured Abe that he would not oppose the launch. It was remarkable that China and Saudi Arabia, with their restrictive approaches to international e-commerce and state-controlled approaches to privacy, joined the United States and the other G7 members to launch trade liberalization negotiations in the sector that will dominate international trade and the global economy in the years to come.

A second advance on digitalization came in the security sphere. At Osaka, G20 leaders added a new thrust to their long-standing global security governance [Kirton, 2017]. They adopted, in a stand-alone statement, an Australian initiative, supported strongly by Russia, to combat the use of social media for the radicalization, recruitment, financing, or planning of terrorism, the deadly effects of which had just been seen in the attacks in Christchurch, New Zealand and Sri Lanka.

### ***Health***

On health, the Osaka leaders did well relative to their past performance. Their 14 commitments were the third highest among G20 summits to date. The G20 encouraged all developing countries to adopt universal health coverage, highlighted as SDG 3 Target 8, in the near term, and to rely on their domestic resources to finance it as a driver of their own development by 2030. To reinforce the thrust, G20 ministers of health and finance met for the first time on the sidelines during the summit itself. Yet the leaders did nothing to anticipate or prevent the COVID pandemic that was to erupt before the year was out.

### ***Climate Change and the Environment***

Osaka's greatest failure came on climate change. It did launch the first global regime to curb plastic and other waste in the world's oceans. This regime would begin with coordinated G20 government action to define the problem, gather reliable data on how much plastic and other waste enters the oceans, determine from where and to what effect, and would then share solutions to reduce and ultimately remove it. G20 leaders also launched the Osaka Blue Ocean Vision to reduce additional marine plastic litter pollution to zero by 2050.

However, on the climate crisis itself, G20 leaders merely prevented a retreat from the meagre consensus reached at Buenos Aires. Nineteen G20 members reaffirmed their intention to implement the 2015 Paris Agreement and improve their commitments there. The United States repeated its intention to withdraw from the Paris Agreement and extolled U.S. accomplishments in promoting clear energy technology and reducing greenhouse gas emissions. No G20 leaders promised new measures to confront the climate crisis already at hand. The entire G20 did repeat the historic commitment from the 2009 Pittsburgh summit to phase out inefficient fossil fuel subsidies in the medium term. Yet, it ignored the fact that the G20 had failed to comply with this commitment by the 2014 due date. Moreover, it added a new condition – “subsidies that encourage wasteful consumption” – that diluted the strength of the original commitment.

This failure on climate change presents a puzzle for the systemic hub model of G20 governance. There were high levels of the model's first key cause – shock-activated vulnerability in the field of climate change and the environment, but low G20 performance as a result [Kirton, 2013].

Japan from the start had given climate change and natural disasters a place on the Osaka agenda, spurred in part by the typhoon that had flooded and closed the Osaka airport in 2018 and the tsunami that had devastated Fukushima and created a nuclear threat in 2011. Awakening these memories was a 6.7 magnitude earthquake in Niigata on 18 June 2019 [Sugiyama, 2019]. Japan set new record highs for heat in early June 2019.

In spring 2019 the United States had historically high and damaging floods in its Midwest farm belt. In June 2019, unusually strong heat waves hit Russia's Siberia, India, Poland and France. Canada's western provinces were struck by an escalating wave of wildfires. In the same year Germany experienced its highest average temperature on record, causing it to shut down a nuclear reactor as a precaution [Batchelor, 2019].

At Osaka, Russian president Vladimir Putin noted the escalating costs of climate change, reversing his position expressed at an Arctic forum in 2017 where he had highlighted the benefits of climate change [The Economist, 2019]. Russia was now warming more than twice as fast as the global average. The number of severe weather events identified by Russia's weather service had risen from 141 in 2000 to 580 in 2018. Yet, in 2019 only 55% of Russians believed humans caused climate change, as they had for the previous decade. They ranked climate change ninth among their main concerns, giving the economy and corruption the top spots.

These visible, directly felt, harmful extreme weather events gave growing public credence to the alarming scientific findings highlighted in the 2018 Intergovernmental Panel on Climate Change report [Hoegh-Guldberg et al., 2018]. The findings showed rising emissions passing a tipping point, leaving only a dozen years at most to prevent the possible extinction of human life. In 2019 a similarly credible report showed severe, unprecedented biodiversity loss [IPBES, 2019].

Adding more visibility were the soaring and spreading mass protests and strikes over climate change. Inspired by 16-year-old Greta Thunberg, student strikes spread across Europe and beyond. The Extinction Revolution movement partially shut down the centre of London and the global financial services centred there. *Our Planet*, the compelling documentary series produced by Sir David Attenborough, rendered publicly visible to many the damage from plastics to the oceans and their fish.

Energy shocks also arose. Between January and April 2019, the world oil price for Brent Crude spiked by 40% to surpass \$75 a barrel. It was widely expected to rise further in the following months due to shutdowns in Venezuela and Libya, and the U.S. decision in late April to end all legal oil exports from Iran. The oil price spiked again, and a new supply cut-off emerged, with the attack on two oil tankers in the Gulf of Oman on 13 June.

## Preparations and Prospects for Saudi Arabia's Riyadh Summit in 2020

The prospects were more promising for the G20's Riyadh summit on 21–22 November, given the Saudi Arabian host's priority agenda and incentives as 2020 unfolded.

### ***Priority Agenda***

For Riyadh, Saudi Arabia's initial approach had been outlined by Crown Prince Mohammed bin Salam to his fellow leaders in the final session of the Osaka summit. Of his 13 agenda priorities, five were economic: the multilateral trading system and WTO reforms; taxation in the digital economy; economic inclusiveness and fairness; the encouragement of entrepreneurs and small- and medium-enterprises; and infrastructure, artificial intelligence, and the Internet of Things. Three were social: youth and women's empowerment; investment in human capital and skills; and future work, up-skilling and re-skilling. One was related to security: cybersecurity, data flow, and science. Five priorities were ecological: climate change and emissions reductions; financing for the SDGs; food security; energy and water access; and water security and sustainability globally and particularly in the Middle East. Leaders would also address the G20's inherited, built-in agenda, including international health.

Ecological priorities and climate change itself had an unexpectedly premier position. The sixth priority was climate change and emissions reduction, presented directly and in their own right. This was a clear reversal from the agendas of the G20 and G7 in 2019, both of which had downplayed climate change due to the actual and anticipated opposition of U.S. president Donald Trump.

These priorities were intensified and expanded when Saudi Arabia outlined its plans on its official G20 website, launched on 1 December 2019 with the formal start to Saudi Arabia's year as host [G20 Saudi Arabia, 2019]. Its overall theme was "Realizing Opportunities of the 21st Century for All." The three pillars of its agenda were "Empowering People," "Safeguarding the Planet" and "Shaping New Frontiers."

The 22 priorities, for the first time in G20 history, put the natural environment first [Kirtton, 2019c]. The six priorities identified under "Safeguarding the Planet" were managing emissions for sustainable development, combating land degradation and habitat loss, preserving the oceans, fostering sustainable and resilient water systems globally, promoting food security, and cleaner energy systems for a new era.

Environmental components also arose directly in three priorities (sustainable development, tourism, and space) under the other two pillars. This offered a foundation for an ecologically mainstreamed, synergistic, multiple benefits approach. "Empowering People" started with scaling up efforts for sustainable development, including SDG implementation and accountability, and contained tourism, including its environmental impact, along with the priorities on education, health, women and youth, tourism, and trade and investment. "Shaping New Frontiers" started with promoting space cooperation, including to "contribute significantly to the protection of common global goods such as climate and the oceans" and continued with the priority areas of digital economy, tax, infrastructure, cities, financial technology, and corruption [G20, 2019].

### ***The Initial Meetings in December 2019***

These prospects were strengthened by the discussions at the first preparatory sherpa meeting, held in early December in Riyadh. Sherpas easily accepted the very broad, well-prepared and quite innovative Saudi priorities. It seemed that the three issues of climate change, trade, and digitalization would dominate the summit.

On climate change and the integrally related energy issue, Saudi Arabia offered the apparently strong solution of a circular carbon economy, which all partners could embrace. It included removing and recycling emissions and ensuring an energy transition to a cleaner, greener result. This well-regarded pragmatic approach allowed partners to advance their priorities, including cleaner fossil fuel technologies, which are expected to dominate the energy mix for the next 10–15 years, and which therefore need to be made cleaner. Tourism was welcomed as a priority pragmatically driven by Saudi Arabia's desire to diversify its economy away from its heavy reliance on oil and gas. The sherpas also discussed water management for agriculture. There was no mention or discussion of the priority of space.

On health, the Saudi approach had considerable support. It featured value-based health care, digital health and patient safety.

Digitalization was a cross-cutting issue that elevated the priority of the digital economy and cybersecurity. It was central to the infrastructure priority, as the Saudis for the first time advanced the concept of "infrastructure" or the digitalization of infrastructure. It was seen as a way of attracting finance, improving human health and enhancing the ecology.

### ***Incentives for Success***

As the Saudi year as host unfolds, several incentives have spurred the Riyadh summit to likely success on the new globalization issues of climate change and, above all, health.

A first incentive is the increasing ecological stress on Saudi Arabia and its neighbours created by climate change. Heat intensified by climate change has been high and rising. It spiked to approach levels in some parts of Saudi Arabia and its neighbours with which the human body cannot not physiologically cope. Climate change has also reduced the availability of fresh water, and harmed agriculture and health in many ways. Such ecological stresses intensified by climate change are also rising in the other Muslim majority members of the G20, including Indonesia, which joined Saudi Arabia as a key member of the Organisation of Islamic Cooperation.

A second incentive is the desire of the Saudi government to diversify its economy away from the hydrocarbons that currently dominate toward a wide array of sectors as outlined in its 2030 strategy [Jalilvand, Westphal, 2018; Kingdom of Saudi Arabia, 2016]. These include the priorities of “Living Healthy, Being Healthy,” “Achieving Environmental Sustainability,” “A Renewable Energy Market,” and promoting sectors such as tourism. Pursuant to this strategy, on 29 September 2019, the new Mutjadedda facility at the Saudi Industrial Development Fund started receiving applications for 1.2 billion riyals’ worth of loans for those wishing to create renewable energy facilities or manufacturing components and those wishing to use their products [Nereim, 2019].

A third incentive is the transformation of the global energy market, with the United States emerging as the first-ranked producer, and the growing shift from hydrocarbons to renewables. Here, Saudi Arabia has the potential to be a solar energy superpower. Its long coastlines offer abundant opportunities for offshore wind and tidal power. The devastating missile strike on the key Aramco oil production sites in September 2019 showed that a vulnerable Saudi Arabia cannot not rely on its oil production and exports for its energy security and economic growth, even in the short term.

A fourth incentive is the diminishing political support from a climate change-denying Donald Trump and his fellow Republicans in the United States. They face re-election on 3 November 2020, immediately before the Riyadh summit is scheduled to start. The U.S. president could arrive at the Riyadh summit as a lame duck, or with less congressional support than he had at the start of Saudi Arabia’s year as G20 host.

### **Support From the UN’s 2030 Agenda and the SDGs**

Further support for a focus on climate change control and environmental sustainability at the Riyadh summit comes from the increasing action to implement the UN’s 2030 Agenda for Sustainable Development and the SDGs (see [Warren, 2019c]). Unlike the preceding eight millennium development goals, with three dedicated to the traditional development priority of health, the 17 SDGs are much more ecologically focused. The seven dedicated to ecological sustainability are SDG 13 on climate, SDG 6 on water, SDG 7 on clean energy, SDG 11 on sustainable cities and communities, SDG 12 on sustainable production and consumption, SDG 14 on sustainable oceans, and SDG 15 on terrestrial ecosystems and biodiversity. The G20 had long governed most of these seven to varying degrees, and many of the other related SDGs as well (see Appendix D).

Moreover, the UN has already moved to mount more summits dedicated to climate change, rather than waiting to do so only at the half-decade intervals as it has been since 1992. In particular, the G20’s Riyadh summit will build on the results of the unprecedented cluster of five UN summits which took place in New York in September 2019. These began on 23 Septem-

ber with the climate action summit (to which over 63 country leaders came, including Donald Trump, who made a brief appearance to hear German chancellor Angela Merkel and Indian prime minister Narendra Modi speak) and the high-level meeting on universal health coverage. They continued with high level meetings on financing for development, SDG implementation, and small island developing states (SIDS) a few days later.

UN Climate Change was scheduled to hold COP26, the 26th conference of the UN Framework Convention on Climate Change (UNFCCC), at the leaders' level in Glasgow, Scotland on 9–19 November 2020, ending the day before the Riyadh summit starts. Leaders were due to make stronger commitments on climate change control than the inadequate ones they made at the Paris summit in December 2015. They would be spurred to do so by the failure of COP25 in Madrid in December 2019, which was unable even to agree on the rulebook needed to launch a global carbon trading system. However, due to the COVID-19 crisis engulfing the United Kingdom by late March, UN Climate Change postponed the Glasgow summit until 2021. It is thus left to the G20 Riyadh summit to make the necessary advances.

## The COVID-19 Crisis and the 26 March Emergency Summit

By far the greatest spur to success at Riyadh is the proliferation of the deadly and destructive crisis in January 2020, the resulting G20 ministerial meetings for health, finance, and energy, and the convening of the first G20 emergency summit, held by videoconference on 26 March [Kirton, Warren, 2020]. At the latter, G20 leaders, in their 1,494-word, 30-paragraph statement, admirably put health first. They opened by declaring that “the unprecedented COVID-19 pandemic is a powerful reminder of our interconnectedness and vulnerabilities” [G20, 2020]. They then declared: “Tackling the pandemic and its intertwined health, social and economic impacts is our absolute priority.” This is a distinctly different message from the one some leaders from the western hemisphere had previously proclaimed when they were home alone, and suggests that they have been converted by G20 summitry to the common, correctly focused cause. They added an empathetic human touch to connect with the people suffering from “the tragic loss of life” and expressed their support to the front-line workers fighting the pandemic. They then promised to do “whatever it takes” to protect lives, safeguard people’s jobs and incomes, and improve people’s economic fortunes.

The first section of the statement, entitled “Fighting the Pandemic,” contains four paragraphs covering a wide range of instruments [Ibid., 2020]. True to the G20’s first focus as an economic and finance forum, the second section on “Safeguarding the Global Economy” offers measures in five paragraphs to minimize the social as well as economic damage, restore growth, and maintain market stability. The third section, on “Addressing International Trade Disruptions,” has three short paragraphs on trade measures to “support the health and well-being of all people.” In the concluding section, on “Enhancing Global Cooperation,” five paragraphs integrate the G20’s health, economic and trade measures, while adding tourism, refugees and migrants, and the security issues of border management and citizen repatriation.

Together the G20 leaders took many important steps. In their principled and normative direction setting, they affirmed the G20’s first distinctive foundational mission of promoting financial stability, but gave more attention to the G20’s second mission to make globalization work for all. On the latter, they specified that they would protect the most vulnerable, send supplies “where they are most needed,” offer “adequate social protection,” “support the health and well-being of all people,” and help developing and least-developed countries, Africa, small island states, and refugees and displaced persons [Ibid., 2020]. On the causal component of the principles they affirmed, they promised to mount a science-based global response, in contrast

to messages heard from some G20 leaders in their instinctive, impromptu, self-confident utterances back home.

In their decision-making, the G20 leaders produced 47 public, precise, future-oriented, politically obligatory commitments, covering a wide range of subjects. They again put health first, with 20 commitments, followed in turn by the global economy with nine, trade with seven, international cooperation with four, financial stability and development with three each, and labour and employment with one. This compares with the performance of G7 leaders in their emergency videoconference 10 days earlier on 16 March which produced 33 commitments, including 21 on health and 12 on the economy, to confront a crisis that was at that time less deadly than it is now.

The 47 commitments made by G20 leaders on 26 March contained many that promised to mobilize new money for health, economic growth, jobs, and development. Here the economy came first, with the headline number of \$5 trillion devoted to this purpose.

To help deliver these decisions, G20 leaders instructed their health and finance ministers to follow up on at regular meetings. These meetings of ministers responsible for a particular subject are the strongest predictor of members' higher compliance with their leaders' related commitments under that same presidency. This thus suggests that greater compliance will come. Compliance with the 75 health commitments that G20 leaders have already made at their regularly scheduled summits averages 73%, so there is a firm basis on which to build.

In the institutional development of global governance, G20 leaders guided their own institutions and those outside in many ways. Inside the G20, they tasked their "Health Ministers to meet as needed to share national best practices and develop a set of G20 urgent actions to jointly combating the pandemic by their ministerial meeting in April" [G20, 2020]. They called for a joint meeting of finance and health ministers in the coming months, an institutional innovation Japan, as host, had pioneered at the Osaka summit in 2019. G20 leaders now also asked their finance ministers and central bank governors "to coordinate on a regular basis to develop a G20 action plan" and declared their support for the Financial Stability Board they had created and control [Ibid., 2020].

Beyond the G20, they made seven references to the WHO, declaring "We fully support and commit to further strengthen the WHO's mandate in coordinating the international fight against the pandemic, including the protection of front-line health workers" [Ibid., 2020]. They followed by guiding the IMF and World Bank Group with three references each, and the Coalition for Epidemic Preparedness and Innovation, Gavi, the Vaccine Alliance, the UN, ILO and OECD with one apiece.

Yet despite this promising start, several shortcomings stand out. First, there was no increase in the permanent base budget of the WHO. Second, G20 leaders did not mandate medical assistance to be provided across borders, nor did they commend the world of non-governmental organizations such as the Red Cross, the Red Crescent, and Médecins Sans Frontières, which selflessly help perform such tasks. Third, G20 leaders did not commit to debt relief for the poorest in a way that could give hard-pressed recipients the funds for health care that they badly need. Fourth, their promise to liberalize trade in health and related goods and services was partial and weak. Even in the section on trade the G20 leaders did not refer to the potential role of the WTO in this regard. Nor did they promise to temporarily suspend some of their members' trade sanctions on Iran, Venezuela and other such countries now struggling with a COVID-19 crisis that could easily spread to their G20 neighbours close at hand. Fifth, there was no reference at all to gender. Sixth, there was no move to make the WHO director-general a permanent member of the G20 summit, as the IMF and World Bank have been from the start. Finally, the G20 leaders thus left much undone as the COVID-19 pandemic escalates in the

coming months. But unlike the G7 leaders 10 days before, the G20 leaders did not promise to meet again the following month to continue their work.

## Strengthening G20 Governance

Given this recent G20 and UN failure on the most complete and threatening form of globalization despite the external shocks and compelling science, the G20 architecture needs strengthening through the following reforms.

The first is to institutionalize the new G20 environment ministers' meeting created in 2019 (see Appendix E). It could be combined with the energy ministers' meeting, with each convening separately and then joining for a combined meeting on their many related concerns. G20 health ministers should also meet more frequently. Such ministerial meetings enhance compliance with the commitments their leaders make on the same subjects at their summit [Rapson, Kirton, 2020].

The second reform is to invite to the summit and the relevant lead-up ministerial meeting the heads of UN Climate Change, UN Biodiversity, UN Environment and the WHO, all of whom have the relevant scientific expertise to shape solutions to these key threats.

The third reform is to invite to the summit and ministerials the leaders of the small countries most rapidly becoming carbon neutral, such as Costa Rica, and those currently most vulnerable to climate change, including the SIDS. They can speak from first-hand experience of their vulnerabilities and solutions, and can expand the representational inclusiveness and legitimacy of the G20.

The fourth reform is to give the UN secretary-general and the director-general of the WHO the same formal status as a G20 member that the heads of the IMF and World Bank have enjoyed from the start. This would match the great broadening of the G20 summit agenda since 2008, including its strong move into the ecological, health, and even political security spheres [Kirton, 2017]. It would also reflect the G20's growing concern with the UN's 2030 Agenda and its SDGs.

The fifth reform is to hold a second annual G20 summit at the UN in September each year. G20 governance was most successful when two summits a year were held, as they were from 2008 to 2010.

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## Appendix A: G20 Summit Performance, 2008–2019

Summit	Grade	Domestic Political Management				Deliberation			Direction Setting				Decision-Making	Delivery		Development of Global Governance				
		Attendance, %	# Compliments	% Members Complimented	# Days	# Documents	# Words	Stability	Inclusion	Democracy	Liberty	# Commitments		Compliance, %	# Assessed	Internal		External		Engagement Groups
2008 Washington	A-	100	0	0	2	2	3,567	16	2	10	2	95	75	8	0	4	39	11	0	0
2009 London	A	100	1	5	2	3	6,155	29	6	9	0	129	57	7	12	4	120	27	0	0
2009 Pittsburgh	A-	100	0	0	2	2	9,257	11	21	28	1	128	67	15	47	4	115	26	0	0
2010 Toronto	A-	90	8	15	2	5	11,078	47	32	11	1	61	68	15	71	4	164	27	0	0
2010 Seoul	B	95	5	15	2	5	15,776	66	36	18	4	153	67	41	99	4	237	31	0	0
2011 Cannes	B	95	11	35	2	3	14,107	42	8	22	0	282	74	22	59	4	247	27	4	2
2012 Los Cabos	A-	95	6	15	2	2	12,682	43	23	31	3	180	77	20	65	4	138	20	7	2
2013 St. Petersburg	A	90	15	55	2	11	28,766	73	108	15	3	281	69	24	190	4	237	27	9	5
2014 Brisbane	B	90	10	40	2	5	9,111	10	12	1	0	205	70	27	39	4	42	12	0	0
2015 Antalya	B	90	0	0	2	6	5,983	13	22	0	2	198	71	24	42	4	54	11	8	6
2016 Hangzhou	B+	95	7	25	2	4	16,004	11	29	34	5	213	71	29	179	4	223	19	14	6

Summit	Grade	Domestic Political Management				Deliberation			Direction Setting				Decision-Making	Delivery		Development of Global Governance					
		Attendance, %	# Compliments	% Members Complimented	# Days	# Documents	# Words	Stability	Inclusion	Democracy	Liberty	# Commitments		Compliance, %	# Assessed	Internal		External	Engagement Groups		
2017 Hamburg	B+	95	0	0	2	10	34,746	42	61	2	11	529	76	26	54	6	307	19	# References		Spread
2018 Buenos Aires	B−	90	0	0	2	2	13,515	23	53	7	2	128	79	20	20	5	24	15	# References		Spread
2019 Osaka	B	95	2	5	2	2	6,623	13	16			143	−	−	56	5	54	17	# References		Spread
Total	N/A	N/A	65	N/A	28	62	187,370	439	429	188	34	2,725	N/A	278	933	60	2,001	289	# References		Spread
Average	N/A	95	4.6	19	2	4.4	13,384	31.4	31	14.5	2.6	195	71	20	66.7	4.3	143	21	# References		Spread

### Notes.

N/A = not applicable. Only documents issued at a summit in the leaders' names are included.

Grade is based on a scoring scheme created by John Kirton, as follows: A+ = Extremely Strong, A = Very Strong, A– = Strong, B+ = Significant, B = Substantial, B– = Solid, C = Small, D = Very Small, F = Failure (including made things worse). See <http://www.g20.utoronto.ca/analysis/scoring.html>.

Domestic political management: participation by G20 members and at least one representative from the European Union and excludes invited countries; compliments are references to full members in summit documents.

Deliberation: duration of the summit and the documents collectively released in the leaders' names at the summit.

Direction setting: number of statements of fact, causation and rectitude relating directly to stability, inclusion, open democracy and individual liberty.

Decision-making: number of commitments as identified by the G20 Research Group.

Delivery: scores are measured on a scale from –1 (no compliance) to +1 (full compliance, or fulfillment of goal set out in commitment). Figures are cumulative scores based on compliance reports.

Development of global governance: internal are references to G20 institutions in summit documents; external are references to institutions outside the G20; engagement groups are references to official engagement groups. Spread indicates the number of different institutions mentioned.

## Appendix B: G20 Performance on Health

Year	Domestic Political Management		Deliberation			Direction Setting		Decision-Making		Delivery		Development of Global Governance	
	Attendance, %	Communiqué Complements	Words		Documents	Financial Stability	Equality	Commitments	% Overall	Compliance	#	In	Out
			#	%									
2008 Washington	100	0	118	3.2	1	0	0	0	0	—	—	0	1
2009 London	100	0	59	0.9	1	0	0	0	0	—	1	0	0
2009 Pittsburgh	100	0	284	3	1	0	0	0	0	—	1	0	0
2010 Toronto	90	0	139	1.2	1	0	1	0	0	—	—	0	1
2010 Seoul	95	0	643	4.1	4	0	1	0	0	—	1	3	2
2011 Cannes	95	0	470	2.9	3	0	1	0	0	—	—	1	0
2012 Los Cabos	95	0	250	1.9	2	0	0	0	0	—	—	0	1
2013 St. Petersburg	90	0	1340	11.2	5	0	2	0	0	—	—	6	4
2014 Brisbane	90	0	769	8.4	3	0	1	33	16	+0.43 (72%)	4	4	9
2015 Antalya	90	0	481	3.5	3	0	1	2	1.7	+0.20 (60%)	2	5	3
2016 Hangzhou	100	0	234	1.4	4	0	0	3	1.4	−0.40 (30%)	1	4	5
2017 Hamburg	100	0	707	2	3	0	3	19		+0.95 (98%)	1		
2018 Buenos Aires	100	0	316	4	2	0	4	4		+0.85 (93%)	1		
2019 Osaka	100	0	934	14	1	0	6	14		—			
Total	N/A	0	6,744	N/A	34	0	20	75	N/A	—	5	23	26
Average	95	0	482	4	2	0	1.4		1.7	+0.45 (73%)	1.3	2.1	2.4

## Appendix C: G20 Performance on Climate Change

Summit	Domestic Political Management		Deliberation		Direction Setting					Decision-Making	Delivery		Development of Global Governance			
	# Communiqué Complements	% Communiqué Complements	# Words	% Words	Financial Stability	Globalization For All	Priority Placement	Democracy	Human Rights	Commitments	Commitments		In		Out	
											Score	% Assessed	Ministers	Officials	# References	# Bodies
2008 Washington	0	0	64	1.7	0	0	0	0	1	0	—	—	0	0	0	0
2009 London	0	0	64	1.0	0	0	1	0	0	3	−0.10 (45%)	33 (1)	0	0	1	1
2009 Pittsburgh	1	5	911	9.7	0	0	4	0	0	3	+0.86 (93%)	33 (1)	4	0	10	5
2010 Toronto	1	5	838	7.4	0	0	0	1	0	3	+0.42 (71%)	100 (3)	0	0	3	3
2010 Seoul	2	10	2,018	12.7	0	0	2	1	0	8	+0.05 (53%)	50 (4)	5	3	20	11
2011 Cannes	2	10	1167	8.2	0	0	0	1	0	8	+0.38 (69%)	37 (3)	2	0	11	7
2012 Los Cabos	0	0	1,160	9.1	0	0	0	1	0	6	+0.59 (80%)	50 (3)	1	5	6	5
2013 St. Petersburg	1	5	1,697	5.9	0	0	1	0	0	11	−0.17 (42%)	27 (3)	0	3	10	7
2014 Brisbane	0	0	323	3.5	0	0	0	0	0	7	+0.51 (76%)	71 (5)	0	0	4	2
2015 Antalya	0	0	1,129	8	0	0	0	0	0	3	+0.70 (85%)	85 (1)	1	1	5	3
2016 Hangzhou*	0	0	1,754	11	0	1	0	1	0	2	+0.58 (79%)	100 (2)	1	3	5	4
2017 Hamburg	0	0	5,255	15	0	0	1	1	1	22	+0.62 (81%)	14 (3)	0	11	26	9
2018 Buenos Aires	0	0	532	6	0	0	0	0	0	3	+0.57 (79%)	79 (2)	0	0	3	3
2019 Osaka	0	0	2034	31	1	1	0	0	0	13	N/A	N/A	1	1	10	9
Total	7	N/A	18,946	N/A	1	2	9	5	2	92	N/A	31	15	27	114	69
Average	0.78	4	1,353	9.3	0.1	0.1	0.88	0.4	0.1	6.6	+0.38 (69%)	69	1.1	1.9	8.1	4.9

*Notes.*

Domestic political management includes all explicit references by name to the full members of the summit that specifically express the gratitude within the context of climate change of the institution

to that member. The % of members complimented indicates how many of the 20 full members received compliments within the official documents, depending on how many full members there were that year.

Deliberation to number of times climate change is referenced in the G20 leaders' documents for the year in question. The unit is the paragraph. % refers to the percentage of the overall number of words in each document that relate to the climate change.

Direction setting, as priority placement refers to the number of times climate change is referenced in the chapeau or chair's summary for the year in question. The unit of analysis is the sentence. The number in parenthesis refers to environment references. Democracy refers to the number of times there was a reference to democracy in relation to climate change. Human rights refers to the number of times there was a reference to human rights in relation to climate change. The unit of analysis is the paragraph.

Decision-making refers to the number of climate change commitments.

Delivery refers the overall compliance score for climate change commitments measured for that year. % assessed represents percentage of commitments measured. The numbers in parenthesis refer to energy commitments.

Development of global governance refers to the number of references to institutions inside the G20 made in relation to climate change. Ministers refers to ministerial groups. Officials refers to official level groups. Out refers to the number of external multilateral organizations related to climate change. The unit of analysis is the sentence.

\*2016 Hanzghou Communiqué reference to climate change-GGA: "We are determined to foster an innovative, invigorated, interconnected and **inclusive** world economy to usher in a new era of global growth and sustainable development, taking into account the 2030 Agenda for Sustainable Development, the Addis Ababa Action Agenda and the Paris Agreement.

## Appendix D: G20 Summit SDG Governance, 2008–2018

Sustainable Development Goal		G20 Subject	Deliberation	Domestic Political Management	Direction Setting		Decisions	Delivery		Development of Global Governance	
					Financial Stability	Globalization for All		Score, %	Number Assessed	Inside	Outside
1	Poverty	Development									
2	Hunger	Food and agriculture	13,098	2			123	73	9		
3	Health	Health	5,810				75	73	9		
4	Education	Education	10,341				5	—	0		
5	Gender	Gender	9,881				55	60	11		
6	Water										
7	Energy	Energy	11,440				157	73	21		
8	Jobs	Labour and employment	28,253				153	75	20		
9	Infrastructure	Infrastructure	9,530				44	90	2		
10	Inequality										
11	Cities	Cities	1,706								
12	Consumption										
13	Climate change	Climate change	16,912				91	69	31		

Sustainable Development Goal		G20 Subject	Deliberation	Domestic Political Management	Direction Setting		Decisions	Delivery		Development of Global Governance	
					Financial Stability	Globalization for All		Score, %	Number Assessed	Inside	Outside
14	Oceans	Oceans	1,827								
15	Land	Biodiversity									
16	Peace/Justice	Regional security									
17	Partnership	International cooperation									

*Notes.*

Compiled by Brittaney Warren, 25 September 2019.

\*Sustainable Development Goals:

1. No Poverty: End poverty in all its forms everywhere.
2. Zero Hunger: End hunger, achieve food security and improved nutrition and promote sustainable agriculture.
3. Good Health and Well-Being: Ensure healthy lives and promote well-being for all at all ages.
4. Quality Education: Ensure inclusive, equitable and quality education and promote lifelong learning opportunities for all.
5. Gender Equality: Achieve gender equality and empower all women and girls.
6. Clean Water and Sanitation: Ensure availability and sustainable management of water and sanitation for all.
7. Affordable and Clean Energy: Ensure access to affordable, reliable, sustainable and modern energy for all.
8. Decent Work and Economic Growth: Promote sustained, inclusive and sustainable economic growth, full and productive employment and decent work for all.
9. Industry, Innovation and Infrastructure: Build resilient infrastructure, promote inclusive and sustainable industrialization and foster innovation.
10. Reduced Inequalities: Reduce inequality within and among countries.
11. Sustainable Cities and Communities: Make cities and human settlements inclusive, safe, resilient, and sustainable.
12. Responsible Consumption and Production: Ensure sustainable production and consumption patterns.
13. Climate Action: Take urgent action to combat climate change and its impacts.
14. Life Below Water: Conserve and sustainably use the oceans, seas and marine resources for sustainable development.
15. Life on Land: Protect, restore and promote sustainable use of terrestrial ecosystems, sustainably manage forests, combat desertification, and halt and reverse land degradation, and halt biodiversity loss.
16. Peace, Justice and Strong Institutions: Promote peaceful and inclusive societies for sustainable development, provide access to justice for all and build effective, accountable and inclusive institutions at all levels.
17. Partnership for the Goals: Strengthen the means of implementation and revitalize the partnership for sustainable development.

## Appendix E: Ministerial Meetings, 1999–2019

Finance	1999–
Employment and Labour	2010–
Tourism	2010–2013
Agriculture	2011, 2012, 2015–2017, 2019
Development	2011
Trade	2012, 2014–2016, 2019
Foreign Affairs	2012, 2013, 2017, 2018, 2019
Energy	2015, 2016, 2018, 2019
Digitalization	2017, 2018, 2019
Health	2017, 2018, 2019
Environment	2019

# The New G20 Politics of Global Economic Governance

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## Abstract

*This article demonstrates how the Group of Twenty (G20) constituted a new G20 politics following the 2008–09 global financial crisis through practices of networked global economic governance. This increased the influence of actors other than officials from leading wealthy states, especially developing- and non-state actors, thus augmenting global governance inclusivity and decentralizing authority. The G20 became the principal hub of global economic governance by influencing and engaging with diverse stakeholders on its broad policy agenda. These networked-governance processes expanded aspects of multilateral cooperation, including transversal approaches to policy issues such as sustainable development. This analysis builds on recent literature on transnational actors, governance networks, and the G20; contributes to emerging constructivist literature on the normative significance of practices and social-relational processes in international relations; and includes a significant discourse-analytic focus on repoliticization and legitimizing discourses. This study indicates, in particular, the political and normative consequences of G20 inclusivity practices for integrating global governance networks.*

**Key words:** authority; depoliticization; G20; global governance; inclusivity; networks; politics; practices; repoliticization; transnational

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## Introduction

This article demonstrates how the Group of Twenty (G20) constituted a *new G20 politics* of global economic governance following the 2008–09 global financial crisis (GFC). It focuses on the international political and normative consequences of networked G20 governance, especially new inclusivity practices for integrating transnational global governance networks, and their broader effects on global economic governance norms and practices.

The analysis is divided into four main sections. The first explicates the analytical framework, which is broadly constructivist but influenced by multidisciplinary research on global governance authority, networks, processes, and practices; as well as depoliticization, repoliticization, and legitimizing discourses. The second section analyzes the significance of explicitly or implicitly *political* practices of global economic governance, especially constituted through repoliticization, despite the former influence of depoliticization practices. The third assesses the politics of networked G20 governance, especially how global governance networks and political contestation influence global governance. The final section focuses on the political and nor-

mative consequences of G20 inclusivity practices, which are important aspects of the forum's networked governance approach.

The forum's networked-governance processes expanded aspects of multilateral cooperation, including transversal approaches to policy issues such as sustainable development. These network processes had important political and normative consequences, especially by decentralizing authority and integrating more heterogeneous actors in post-2008 global economic governance.

## Analyzing the New G20 Politics

This section explicates the analytical approach, which augments current conceptual frameworks for analyzing global economic governance. The present study assesses the G20's significance for contemporary global governance *practices*, foregrounded along with *social-relational processes*, rather than focusing either on macro-structures or individual agency. It argues that the G20 constitutes a new politics of global economic governance through such processes and practices, reinforced by key legitimizing discourses.

The article analyzes the significance of G20 governance networks, while incorporating constructivist insights on the normative consequences of shifting international practices and social-relational processes. This indicates a social-processual and practice-focused approach, fitting David McCourt's categorization [2016, pp. 478–9] of practice-relational constructivism (see [Luckhurst, 2019a]). The empirical focus is how *global governance networks*, which consist of private, intergovernmental, supranational, state, semi-state, and/or non-state actors, influence the new G20 politics of global economic governance. It further indicates the increasing pluralism of the types of actors involved in contemporary global governance.

This analytical approach denotes a broad understanding of politics as involving constellations of practices and processes, through which actors engage in contesting the governance of societies or the world, in the case of global governance and world politics. This study includes a focus on the political and normative consequences of *inclusivity practices* for this new G20 politics, especially how these augmented the influence of more heterogeneous global governance networks since the GFC. It is important also to consider the potential future implications of such normative shifts in global governance, which have reflexive significance for actors' understanding of the contemporary context of G20 politics. The perception that more diverse actors and networks are engaging in global governance could increase demands for inclusion from currently excluded or marginalized actors and networks, on legitimacy and inclusivity grounds.

This networked form of G20 politics is part of the growing trend for increasingly diverse and complex forms of global governance since the 1990s, in terms of organization, actors, and policy areas [Dingwerth, Pattberg, 2006, p. 192; Rosenau, 1992, pp. 1–3]. The United Nations' (UN) 2030 sustainable development goals (SDGs) are a good example of the increasingly complex and transversal contemporary approaches to global governance which substantially influenced the G20's policy agenda. The G20 is congruent with broader shifts in global governance in that it engages with multiple organizations, governance networks, actors, and policy issues. This indicates the forum's function as a global governance hub [Kirton, 2013, pp. 27–52; Luckhurst, 2019b], particularly for the global governance networks that engage with its diverse agenda. This constitutes a new form of world politics, one that is less state-centric and more inclusive of actors other than representatives of leading wealthy states.

This study focuses substantially on the post-GFC inclusion of more heterogeneous global governance networks through engagement with the G20. The latter augmented the influence of more diverse networks on transversal policymaking processes, thus decentralizing global

governance authority. The analytical approach is to examine how such networked governance relations, processes, and practices constituted a *new G20 politics*, through the G20 embedding significant shifts in global economic governance norms and practices.

The G20 and G20-engaged governance networks reciprocally influence each other through shifting processes, relations, and practices rather than unilateral individual agency or macro-structures. This approach is influenced by Emanuel Adler's insights [2019, p. 27 – emphasis in original] on what he terms “cognitive evolution,” and the “*epistemic practical authority*” of some actors to ascribe meaning to practices and “background knowledge” about the world. The notion of epistemic practical authority is similar to other constructivists' emphasis on “cognitive authority” [Broome, Seabrooke, 2015], which the present author integrates in a broader analytical approach to three key dimensions of global governance authority, namely strategic, political, and cognitive authority (see [Luckhurst, 2017]).

Adler [2019, p. 27] asserts that epistemic practical authority “results from processes of epistemic authority contestation between different claims.” He further explains:

international social orders evolve because of the intervention of new social actors and/or the effects that the replacement of one type of political entity and institution by another may have on background knowledge and practices, on the negotiability processes within communities of practice, and on the selection processes between different communities [Ibid., p. 28].<sup>1</sup>

This is useful for understanding the analytical approach of the present study. Global governance practices and background knowledge, the latter being commonplace or taken-for-granted assumptions about the world, *evolve through processes – hence ongoing social relations – of contestation*. Consequently, as Adler notes [Ibid., p. 31], they are “socially-emergent properties rather than individuals' property.” This points to important ontological and epistemological insights which are impossible to examine here in detail (see [Ibid.]). Suffice to note that while G20-engaged global governance actors are capable of reflexivity and agency, their agency is context-dependent and exists within complex social interactions and processes; indeed, *agency occurs through social relations*. Individual actors, moreover, are reflexive but not isolated from the consequences of shifting global governance authority, practices, and background knowledge.

This indicates the significance of the final conceptual issues, the influence of *depoliticization*, *repoliticization* and *legitimizing discourses*. The latter has been analyzed by international relations scholars of critical discourse analysis [de Ville, Orbie, 2014]; and by the present author in researching the G20 and other aspects of global economic governance [Luckhurst, 2016a; 2016b; 2017; 2020]. Legitimizing discourses constitute narratives that are instrumentalized to reinforce actors' authority, in the sense noted by Adler [2019, p. 27], to ascribe meaning to practices and background knowledge about the world. This has authority effects *to the extent that others are persuaded*, since authority is constituted through socially constructed perceptions [Hopf, 1998, pp. 178–9; Reus-Smit, 2007, p. 44]. G20-engaged global governance networks deploy legitimizing discourses in processes of political contestation, in attempting to sway global governance norms and policymaking. “Depoliticization” and “repoliticization” indicate processes of increasing or decreasing political contestation of particular policy issues, incorporating practices such as the use of legitimizing discourses and other techniques to augment authority, ascribe meaning and constitute background knowledge.

<sup>1</sup> “Communities of practice” consist of actors that collectively adhere to particular practices, for example specific policy or diplomatic practices (see [Adler 2008; 2019]). Unlike global governance networks, they do not necessarily cooperate as professionally linked networks.

The new G20 politics of global economic governance is crucially influenced by networks, through practices and processes constituted by and constitutive of social relations, rather than through macro-structures or individual agency. This analysis further indicates the significance of the G20 for important shifts in post-GFC global economic governance. The G20 constituted new processes and practices which, due to its authoritativeness as a global governance hub [Eccleston, Kellow, Carroll, 2015], increased multilateral fora and governments' openness, or permeability, to more heterogeneous global governance networks. This contributed to the ongoing process of decentralizing global governance authority since the 1990s, which accelerated during the GFC. The present article examines the significance of such political and normative shifts.

## Repoliticizing Global Economic Governance

This section analyzes the influence of the G20 on explicitly and implicitly *political* practices of global governance. It includes a brief review of global economic governance since the 1990s. This indicates how the G20, as a crucial hub for global governance networks, established social-relational processes and normative practices that constituted a *new politics* of global economic governance following the GFC. The G20 thus substantially contributed to the recent *repoliticization* of global economic governance.

Here it is useful to reiterate the conceptualization of “politics” and “political” deployed in the article, especially to denote the *contestation of processes and practices of governance*. This points to the agonistic, or contested and contestable, aspect of politics. The G20's hub role in decentralizing global governance authority contributed to diffusing new norms and practices of global economic governance; in doing so, it also constituted new contexts and practices of deliberation, engagement and political contestation on global governance issues such as financial regulation, macroeconomic policies, sustainable development, infrastructure financing, corporate taxation and gender equality [Luckhurst, 2016a; 2019b]. This is not to claim that the G20 alone politicized global governance, since global governance has always been implicitly or explicitly political. The G20's role as a hub for decentralizing global governance authority instead augmented the heterogeneity of political contestation in this context through its inclusion of more diverse organizations, actors and policy issues.

The notion of *governance* became popular during the 1990s, including in domestic and international policymaking. Some scholars subsequently focused on multilevel governance, indicative of the complex interlinkages between more diverse actors and networks across local, national, regional and global governance settings (see [Bache, 2008; Hooghe, Marks, 2001; Sikkink, 2005]). Other scholars focused on the growing influence of non-state actors and networks in global economic governance, such as transnational advocacy networks and civil society organizations (CSOs), on issues such as the International Monetary Fund (IMF) debate on prohibiting capital controls, deliberations on the Organisation for Economic Co-operation and Development's (OECD) Multilateral Agreement on Investment, and on the norms of international trade [Hannah, 2016; Keck, Sikkink, 1999; Scholte, 2004; Smythe, 2000]; while others examined the influence of professional standard-setting bodies and private actors on the governance of international professional practices and product standards [Büthe, Mattli, 2011; Coni-Zimmer, Flor, Wolf, 2019]. This was indicative of key epistemic and normative shifts, from emphasizing the political authority of national *governments* to conceptualizing authority within a more heterogeneous context of *governance*. There are different perspectives on what this implies for politics and political agency. Eva Sørensen and Jacob Torfing [2017, p. 40] contrast what they call “the depoliticizing impact of the public management perspective” on governance, with the “political science perspective” that “repoliticizes” it. The former emphasizes governance as a technocratic space of rational decision-making, the latter as a political

space of continual contestation, especially between a growing diversity of actors. The present article broadly fits within the latter category, focused here on international or global, rather than national, politics.

The repoliticization of global economic governance since the GFC, as an increasingly heterogeneous context of political contestation, occurred despite the influence of recent depoliticization practices (see [Sørensen, Torfing, 2017]). The latter indicated the agency of cognitively authoritative expert actors and governance networks, constituting policymaking spaces that were designed to be perceived as technocratic, thus minimizing broader political contestation of their authoritatively prescribed best practices. This signifier “best practice” was professionally and epistemically reinforced by legitimizing discourses, deployed to justify the exclusive influence of certain groups of experts, especially those from global governance networks with cognitive authority on key economic policymaking areas.

Global governance networks that advocated the so-called Washington Consensus and neoliberal deregulation strategies constituted such discursive depoliticization practices, often successfully, during the 1990s. Officials from the IMF, the World Bank, and Group of Seven/Eight (G7/8) governments emphasized the benefits of markets for economic growth and efficiency [Rodrik, 2006; Stiglitz, 2002; Williamson, 1990]. This influenced public and policymakers’ perceptions of politics and the role of the state. Some centre-left political parties also perceived the apparent failings of state-interventionist policymaking strategies as necessitating an expanded role for markets in society [Driver, Martell, 2000; Giddens, 1998; Jessop, 2003].

Critics of neoliberalism sometimes claimed the growing third sector of voluntary, non-profit organizations could complement the economic roles of the state *and* markets [Evers, 1995]. The declining influence of the public sector around the turn of the millennium more often led to an increasing role for markets. This was due to the growing epistemic and normative sway of rational and public choice approaches to policymaking, influenced by New Classical economics, between the 1980s and early 2000s. This situation persisted until the GFC, especially among global governance networks and politicians in several key wealthy states.

Doubts about market efficiency arguments for economic deregulation and liberalization became increasingly prevalent, though, among citizens and politicians in those developing states that experienced financial crises in the 1990s and early 2000s. This was partly because the crises were particularly damaging in developing states such as Argentina, Indonesia, Mexico and Thailand which had followed economic policy advice from the IMF and other Washington Consensus advocates [Graham, Masson, 2002; IMF, 1996; Rodrik, 2006, p. 975; 2012, p. 119; Stiglitz, 2003, pp. 243–6]. This undermined the cognitive authority of the advocates of the Washington Consensus, especially when the World Bank rejected these policy prescriptions in the early 2000s, while the IMF continued to endorse them. This led to open disagreement between the Bretton Woods sister institutions (cf. [IEO, 2003, p. 6; Rogoff, 2002; 2003; Singh et al., 2005; Stiglitz, 2001; World Bank, 2005]), indicating the earlier institutional normative consensus on economic policymaking in global *development* governance had given way to political contestation by the 2000s.

This apparent *return of the political* in global development governance extended to other aspects of global economic governance during the GFC. The latter was crucial for decentralizing authority in key contexts of global economic governance, such as financial regulation and macroeconomic policy coordination [Luckhurst, 2016a; 2017]. The G20 became significantly more important in global economic governance with its elevation to a leader-level forum at its first summit in Washington DC, in November 2008. The G20’s subsequent expansion to include sherpa meetings,<sup>2</sup> ministerials, working groups, official engagement processes, and *ad*

<sup>2</sup> The term “sherpa” refers to each G20 leader’s personal representative, or chief negotiator, at the forum.

*hoc* meetings enabled it to become a “*hub of decentralizing authority* in global economic governance” [Luckhurst, 2019b, p. 7, original emphasis], establishing new inclusivity practices for incorporating more heterogeneous actors and networks [Ibid., 2019c]. This included its role in expanding the membership of the Basel Committee for Banking Supervision (BCBS) and the new Financial Stability Board (FSB) in 2009 to include representatives from the formerly excluded G20 developing states. There was also greater inclusion of non-state actors through the G20’s official engagement forums. These inclusivity practices were important for the new G20 politics of global economic governance, in substantive policymaking terms, and because of their consequences for normative, political and cognitive authority.

The G20 became a focus for political contestation after the GFC, especially with the growing policy divergence on the core macroeconomic goal to augment the global economic recovery. This took the form of persistent disagreements after 2010 on the relative benefits of fiscal austerity and stimulus policies between the leading European Union states, advocating the former, and the Obama administration, the Chinese government, and increasingly the IMF, advocating the latter. The G20’s collective cooperation during the GFC, especially from September 2008 to September 2009, briefly seemed to indicate the potential for establishing an *ad hoc* form of embedded liberalism (see [Helleiner, 2010; 2019; Luckhurst, 2012]), a partial reversion to the more deeply institutionalized multilateral cooperation of the post-war Bretton Woods system. Combined with the potential for achieving a Bretton Woods-style consensus, such an approach would have constituted new *political practices* of economic governance by creating spaces for political deliberation and coordination to achieve socioeconomic goals and reduce negative effects from global macroeconomic imbalances. The G20 accomplished some of these through aspects of its GFC-period coordination, though with more modest achievements since 2010. It subsequently remained a hub of decentralizing global governance authority [Luckhurst, 2019b] despite the post-GFC political and economic constraints. The G20 broadly sustained the status achieved at its Pittsburgh summit of September 2009, when members proclaimed it “the premier forum for our international economic cooperation” [G20, 2009b]. The G20 continued this coordinating role with diverse actors, governments, and international organizations such as the FSB, the IMF, the World Bank and the OECD [Callaghan, 2017; Larionova, 2017; Lesage, 2014; Wouters, van Kerckhoven, 2011].

Despite the growing macroeconomic policy divergence after 2010, G20 inclusivity practices increased the influence of actors other than officials from leading wealthy states. This enabled the leading developing states to make more substantial financial and policy-normative contributions to multilateral cooperation, while also being more inclusive of non-state actors in policy deliberations. These practices were *political*, both in terms of their consequences for the expanded deliberation and contestation of governance practices, and their significance for shaping the processes and policy outcomes of global economic governance.

Trade issues, like economic development, also became more prominent in G20 deliberations after the GFC. The main concern on trade in the immediate aftermath of the GFC was to avert protectionism; this was influenced by the common belief that protectionism had exacerbated the 1930s Great Depression. It was another key policy area that became repoliticized in recent years, especially after Donald Trump won the U.S. presidential election in 2016. Trump’s confrontational and protectionist measures in response to what he claimed were unfair trade practices from several states, especially China, put an end to the erstwhile *rhetorical* consensus at the G20 – by which the forum had consistently reiterated its anti-protectionism pledge at its annual summits. Simon Evenett [2013] had argued that G20 states failed to fulfil their anti-protectionism commitments anyway, but Trump’s willingness to break with the politico-rhetorical commitment to anti-protectionism was indicative of the normative repoliticization of international trade practices.

## The Politics of Networked G20 Governance

The G20 influenced the global economic architecture through significant new political *and networked* governance practices [Baker, Carey, 2014; Eccleston, Kellow, Carroll, 2015, pp. 301–3; Luckhurst, 2019c]. The greater pluralism and complexity of post-Cold War global governance, in terms of organization, actors and policy issues, augmented the authority and influence of more heterogeneous actors. This was possible through their inclusion in global governance *networks*, because agency is constituted through social relations.

The focus here on global governance networks, rather than broader civil society inclusion, indicates the limits of this form of inclusivity. G20-engaged global governance networks are heterogeneous but often consist of professional-expert and elite actors [Luckhurst, 2019c; Stone, 2015]; hence, not only state representatives, but also *not all citizens*. These networks often provide links to broader groups and civil society, however, thus increasing the scope for policy engagement and public diplomacy. G20 sherpas play a significant role in this context, as they communicate with the diverse interlocutors and engagement groups, constituting practices of inclusivity and socialization [Luckhurst, 2019; Rewizorski, 2017, pp. 42–5]. The official G20 engagement fora constituted key practices of inclusion, in addition to those constituted through G20 engagement with non-member states and its inclusion of developing states, which augmented their influence on global economic governance.

The G20's policy agenda during the GFC was mainly focused on the perceived immediate threats, especially the need to recover from the economic downturn, but also on reforming global financial regulation to prevent a repetition of the crisis. Despite the narrow focus of the economic governance agenda, there were significant shifts in terms of authority, norms and practices. One was the greater integration of G20 developing states in global economic governance bodies, especially the FSB and the BCBS. Another crucial example was the increasing influence from the global governance network on macroprudential financial regulation. This shifted the G20's agenda on financial-sector regulatory reforms during the GFC, leading G20 members to endorse macroprudential regulation [G20, 2010].

Before the GFC, the prevalent financial regulatory framework advocated by leading western-based officials had been *microprudential* regulation. This emphasized the role of individual firms' internal monitoring of financial-regulation compliance, with a greater focus on individual firms' performance than on potential sectoral-level problems. For several years before the GFC, critics of the microprudential approach had advocated more monitoring and regulation that addressed sectoral risks, through macroprudential financial regulation. This indicated a focus on "factors that could endanger the financial system as a whole, even if they would not be obvious as serious threats when viewed in the context of a single institution" [Elliott, 2011]. The shift to macroprudential regulation had been advocated, especially, by staff from the Bank for International Settlements (BIS) for several years before the GFC (see [BIS, 1986; Crockett, 2000]). The latter undermined aspects of the erstwhile conventional wisdom in global governance circles such that the global governance network advocating macroprudential regulation managed to supplant the epistemic and normative influence of the microprudential approach [Baker, 2013; Luckhurst, 2016a, pp. 149–56; 2017, pp. 92–7]. This global governance shift was substantially influenced by the macroprudential governance network, with coordinated advocacy from officials at the BIS, the FSB, and the IMF (see [FSB, IMF, BIS, 2011]), plus among national policymakers such as financial regulators, central bankers, and staff at finance ministries. The G20 became a crucial global governance hub for steering the macroprudential shift in financial regulation, especially through the forum's instigation and endorsement of the new Basel III Accords in 2010 (see [BCBS, 2010]). This role was particularly influenced by the G20's Working Group on Enhancing Sound Regulation and Strengthening Transparency

which, notably, was co-chaired by the Canadian representative Tiff Macklem and the Indian representative Rakesh Mohan. This combination of key actors from the Global North and Global South further indicated the greater heterogeneity of post-GFC, G20-engaged global economic governance networks.

The macroprudential financial-regulatory shift was *not purely* the result of state agency. It was influenced through broader networked actors and practices of global governance advocacy and authority. Moreover, it was not simply a technocratic process; instead it had important political repercussions for global and domestic financial governance, as well as epistemic and normative consequences. It constituted political shifts in the setting of new regulatory practices. Importantly, this undermined the cognitive authority of policymakers who had advocated decreasing financial regulation to facilitate supposedly rationally efficient market practices, due to their assumption of potential efficiency gains. This had broader political repercussions, including further refuting the prioritization of deregulation and market liberalization in development policymaking, under the influence of the former Washington Consensus. This reinforced the shift in development policymaking to a growing sustainable development consensus.

G20 macroeconomic governance also was substantially influenced by epistemic, normative and policymaking shifts during the GFC. The intergovernmental dissensus between G20 members, noted earlier, was reinforced by contestation between competing communities of practice and global governance networks on how to achieve a global economic recovery, especially advocates of fiscal stimulus versus austerity advocates. There was a Keynesian revival during the GFC [Farrell, Quiggin, 2017; Luckhurst, 2012] which influenced the G20's macroeconomic agenda and agreements in 2009, especially its support for a fiscal stimulus and collective growth-oriented economic policies [G20, 2009a; 2009b]. This was followed by growing contestation from 2010 onwards as advocates of fiscal-austerity measures gained greater sway. These competing networks and practice-communities included diverse actors engaged in political contestation of competing claims on the best approach to macroeconomic governance. The brief resurgence of Keynesian policymaking strategies during the GFC was only possible due to the existence of actor-networks that could influence the G20 and global economic governance once a crisis effect undermined the influence of recent macroeconomic policy norms and practices (see [Widmaier, Blyth, Seabrooke, 2007]). The advent of a new crisis at the end of 2009 and start of 2010, specifically the Greek and then subsequent eurozone crisis, similarly gave austerity advocates an opening to contest the Keynesian emphasis on fiscal-stimulus policies. This included non-state actors contributing to the contestation in favour of austerity, for example Alberto Alesina and Silvia Ardagna [2009] and Carmen Reinhart and Kenneth Rogoff [2010]. Alesina was particularly influential in the European Union's political debate on austerity and fiscal stimulus. He gave a presentation [2010] on his claims about the benefits of austerity, or "fiscal consolidation," to the European Union's Finance Ministerial meeting (Ecofin) in April 2010.

Heterogeneous groups of state and non-state actors were also involved in global governance networks in other policy areas. A global sustainable development governance network, linked to the broader community of practice on sustainable development, significantly influenced the post-GFC G20 agenda. This had important policy consequences for global development governance, though the G20 was relatively less influential as a global governance forum in this policymaking context. It constituted, instead, a collaborative governance hub to complement the efforts of the UN and World Bank on sustainable development governance. Global authority shifts during the GFC, indicated by the G20's growing inclusivity practices [Luckhurst, 2019c], gave greater influence to the G20's developing-state members but also, significantly, to newly industrialized Republic of Korea. The latter's post-GFC augmented authority was indicated when it became the first non-G8 member, and first non-Anglosphere state, to

chair the leader-level G20 in the second half of 2010. This example of decentralizing global governance authority initiated the G20's agenda expansion over subsequent presidencies, due to the Koreans introducing development issues, which crucially influenced the forum's role and broader global governance norms and practices.

The Korean G20 Presidency was influenced by actors from the global sustainable development governance network, especially those from the influential CSO Oxfam. Oxfam lobbied the Koreans to include development issues in the G20 agenda, thus expanding it beyond the GFC-period focus on economic recovery and financial reform. The Koreans adopted the phrase proposed by Oxfam [2010], "Seoul Development Consensus," as the label for their G20-chair development proposals [G20, 2010]. The latter rejected the prescriptivism of the defunct Washington Consensus and endorsed more sustainable development practices, including a strategic development role for the state.

The Korean G20 Presidency made these proposals in a broader context of shifting global development governance authority. The World Bank [2005] had already abandoned the Washington Consensus before the GFC; others, as noted earlier, also rejected the core macroeconomic principles underpinning the Washington approach, particularly after the Asian financial crisis and during the GFC. Cognitively authoritative actors, such as leading economists and development experts Dani Rodrik [2001], Jeffrey Sachs [2015], Amartya Sen [2013], and Joseph Stiglitz [2002] were part of a broader community of practice on sustainable development that contributed to legitimizing the political shift to sustainable development. The normative and cognitive authority shifts were influenced by the aforementioned political contestation on financial and macroeconomic governance, and by a global sustainable development governance network of intergovernmental, state and non-state actors. These authority shifts swayed the G20's post-GFC development agenda, with the forum's own Development Working Group (DWG) helping to coordinate and consolidate the G20 governance network on sustainable development.

Subsequent G20 presidencies continued to incorporate sustainable development in their agendas [Berger, Leininger, Messner, 2017, pp. 120–1], with the G20 endorsing and advocating the UN's SDGs through their leaders' summit declarations [G20, 2015; 2016a; 2017; 2018; 2019]. The 2016 Chinese G20 Presidency and its Hangzhou summit further consolidated the coordinating role of the G20's DWG in its sustainable development governance network, as emphasized in its post-summit document, "G20 Action Plan on the 2030 Agenda for Sustainable Development" – the latter also noting the importance of G20 cooperation with civil society and the official G20 engagement groups [G20, 2016b, pp. 14–5; Scholtz, Brandi, 2017, pp. 157–8]. Oxfam and other CSOs have continued to play a significant lobbying and engagement role, including through the official Civil 20 engagement forum that was inaugurated during the Russian G20 Presidency in 2013. This influence of the G20 sustainable development governance network was indicative of the expanded agenda and the heterogeneity of networks involved in the new G20 politics of global economic governance.

In the context of global development and financial regulation, G20 networked governance resulted in the shift to a new policymaking consensus. However, the new G20 politics of networked governance does not always result in comprehensive policy shifts or normative consensus. The macroeconomic *dissensus* since the eurozone crisis, especially, was influenced by competing governance networks, respectively, advocating austerity or fiscal-stimulus policies, such that the G20 was unable to maintain the level of cooperation on macroeconomic policy strategies that occurred during the GFC. There has also been divergence from the Trump administration, more recently, in rejecting the broad consensus among most G20 members on trade and climate norms. This indicates the significant contestatory aspect to the new G20 politics, with global governance networks at the core of macroeconomic political contestation.

## Political and Normative Consequences of G20 Inclusivity Practices

The G20's hub role influenced the repoliticization of networked global economic governance during the GFC. New G20 inclusivity practices contributed to the diversification of actors and networks involved. This had broader political and normative consequences, constituting the important normative shift to a process of growing legitimization through the expansion of inclusivity practices in global economic governance.

Analysis of G20 networked-governance processes indicates their substantial political and normative repercussions, also, in expanding the scope of the forum's multilateral cooperation. The G20's post-GFC policy agenda expanded considerably by incorporating issues such as the SDGs and a growing emphasis on complex, transversal policy strategies. This was due, in large part, to political contestation and advocacy from newly included actors and networks in G20 governance processes, therefore a significant consequence of these inclusivity practices. The Korean G20 Presidency, during the second half of 2010, had the crucial normative consequence of initiating the agenda expansion that continued during subsequent G20 presidencies. Advocates of this broader agenda were able to articulate it with the signifier "legitimacy," thus constituting a normative trap [Schimmelfennig, 2001] by rhetorically linking the expanded G20 agenda, including issues of sustainable development, with legitimacy. This was because the expanded agenda was advocated by representatives of developing states, so the increasing discursive imbrication of *global governance legitimacy* with *inclusivity* undermined the capacity of G7/8 governments to ignore the priorities of developing-state governments; hence the former were less able to dominate the G20 policy agenda [Luckhurst, 2019c].

More recently, global governance networks have influenced G20 policy deliberations on broader, transversal issues such as gender equality. The official G20 engagement forums have been influential in this context. The C20 successfully lobbied the 2014 Australian G20 Presidency to incorporate the goal of reducing the gender labour-participation gap in the G20, by 25% by the year 2025 within the Brisbane summit leaders' declaration [Harris Rimmer, Byrne, 2019, p. 174; see C20, 2014; G20, 2014]. More recently, the Osaka G20 summit declaration [G20, 2019] integrated key gender-equality priorities advocated by the engagement forums, especially in two pre-summit joint statements from the C20, L20, T20, W20 and Y20 [2019a; 2019b], one on the gender labour-participation gap and the other on eliminating work-based violence and harassment.

This points to the normative influence from the G20 gender-equality governance network, partly because gender issues were not initially emphasized by the Japanese G20 Presidency. It further indicates how the expansion of G20 policy and political engagement practices contributed to the new G20 politics. The growing inclusion of global governance networks engaged across the expanded G20 agenda increased their capacity to lobby and influence the forum. This further contributed to the development of new "constructed focal points" for cooperation on these broader agenda issues [Keohane, Martin, 1995, p. 45], providing opportunities for such issues to be foregrounded in global governance deliberations. The G20's official engagement processes, in particular, compel the forum members *to engage*, further augmenting the imbrication of legitimacy with inclusivity practices.

There has been substantial scholarly debate on the G20's agenda expansion [Luckhurst, 2016a, pp. 190–6]. This has often been framed in the language of a depoliticizing efficiency discourse versus a repoliticizing legitimacy discourse, the former deployed to advocate more restrictions on inclusivity and the latter to advocate existing or additional inclusivity practices (cf. [Carin et al., 2010; Cooper, Momani, 2014; Slaughter, 2013]). This is a crucial debate in the politics of networked G20 governance; ostensibly about contesting best practice in G20 govern-

ance, it has become a core political divide between networks and actors engaged in the new G20 politics. G20 inclusivity practices contributed to the repoliticization of key aspects of global economic governance, as noted, especially because they expanded the actors engaged and the policy issues and options debated since the GFC. This repoliticization of key aspects of the extended G20 agenda, influenced by inclusivity practices, constituted new normative practices which could be deployed for purposes of global governance legitimization.

The evidence of networked G20 governance indicates the forum's permeability to heterogeneous global governance networks, by contrast with traditional approaches to diplomacy and multilateral economic fora which have tended to be more state-centric and involving exclusionary practices. In this sense, post-GFC authority shifts constituted a new G20 politics of global economic governance in terms of the scope of policy deliberations and practices, plus the greater pluralism and diversity of networks and actors involved. This constituted new inclusivity practices with important political and normative consequences for global economic governance. The new inclusivity practices also had significant effects on the leverage from states' strategic authority, effectively undermining the capacity of key states, for example the G7 members, to dominate the G20 agenda and global governance processes [Luckhurst, 2019c, p. 533]. G20 practices contrasted with the much weaker forms of engagement and inclusivity introduced by the G8 before the GFC, such as the Outreach Five engagement through invitations to the leaders of Brazil, India, China, Mexico and South Africa to attend G8 summits as guests, with the areas of engagement dictated by the G8 [Cooper, Thakur, 2013, pp. 59–62; see Peters, 2019]. These measures had occurred before the elevation of the G20 to a leader-level forum.

The pre-GFC hierarchy in global economic governance engendered a sense of inequality and injustice among several policymakers in leading developing states. This was evident from various public statements, which indicated the normative and political significance of the G20's inclusivity practices. Policymakers from leading middle-income states, especially, were dissatisfied with the pre-GFC hierarchy in global economic governance. Guido Mantega, the Brazilian finance minister in 2008, noted the Brazilian delegation at the first G20 summit would not be attending just to be "mere coffee drinkers" [Partlow, 2008] and wanted to be fully engaged in policy deliberations. Chinese and Indian policymakers made similar comments [Cooper, Farooq, 2013, p. 430; Paulson, 2015, p. 240]. These kinds of statements indicated the important political and normative consequences of the G20's inclusivity practices. Eric Helleiner [2016] noted these practices increased the potential for "cooperative decentralization" by linking compatible Bretton Woods institutional practices with those of new BRICS-based institutions such as the New Development Bank,<sup>3</sup> and with post-GFC regional projects such as the Chiang Mai Initiative Multilateralization and the Asian Infrastructure Investment Bank. Cooperative decentralization reduced the likelihood of global economic governance fragmentation into competing organizational architectures, thus contributing to decentralizing strategic, political and cognitive authority rather than splits, especially between BRICS and G7 countries [Luckhurst, 2017, pp. 219–40].

G20 inclusivity practices could have significant political and normative consequences for member- and non-member- states' domestic economic governance, especially through their influence on understandings of sovereignty and political inclusivity. The new G20 politics of increasingly *inclusive and networked* global economic governance provides opportunities for interlocutors to engage in the forum's policy debates, increasing their potential influence in this context. There could also be domestic political effects to the extent that more heterogeneous G20 governance networks could use their augmented international influence, directly or indirectly, to sway domestic policymaking practices and political norms of civil society engagement. This could further undermine state-centric understandings of sovereign authority by normatively legitimizing the role of heterogeneous actor-networks in contemporary governance.

<sup>3</sup> BRICS = Brazil, Russia, India, China, South Africa.

The present article indicates the limited influence of states' strategic authority in a world of increasingly complex, pluralist, and networked governance, where key policy issues are contested by competing governance networks linked through often transnational professional ecologies [Karlsrud, 2016; Luckhurst, 2019c; Seabrooke, 2014]. Even in those states, such as the BRICS members, where governments prioritize sovereign authority and independence, sovereignty does not equate homogeneity or uniformity among policymakers. Competing policy communities and governance networks exist, domestically and among official representatives at multilateral bodies and other domestic global-governance stakeholders, as indicated by David Shambaugh's [2013] analysis of policy divergence between Chinese policymakers. This was evident during the global financial crisis, when Chinese domestic and global governance actors differed on key issues, such as whether China should introduce capital-account liberalization and whether the international reserve-currency role of the U.S. dollar should continue [Davis, Wei, 2013; Luckhurst, 2016a, pp. 69, 225]. Economic policy discourses are influenced by domestic political contexts but are often borderless in terms of the international prevalence of transnationally shaped debates on topics such as digitalization, globalization, gender economic equity and sustainable development.

The new G20 politics crucially expanded the scope, actors and networks engaged in broader contexts of global economic governance. This might undermine resistance to expanding inclusivity processes and practices in other areas of global governance, including security, perhaps even at the UN Security Council. This is only one potential scenario; complex political and diplomatic concerns would be involved in any such shift at the UN. For the moment, while the new G20 politics of heterogeneous and networked global economic governance incorporates an extensive agenda of important issues with sovereignty implications, including digital technology, migration, infrastructure and other transversally linked topics; military security arguably remains the most obvious state-centric dimension of global governance (see [Alexandrov, Stein, 2019]).

## Conclusion

The new G20 politics of global economic governance since the GFC had crucial consequences. It established important new inclusivity practices which substantially augmented the post-crisis influence of more heterogeneous global governance networks. These broader networks included more actors from developing states, as well as non-state actors. This also influenced the G20's agenda expansion, especially after 2010.

The first section introduced key aspects of the analytical approach, including the focus on how inclusivity practices and decentralizing authority were influential in constituting more heterogeneous G20 governance networks. The second section indicated the significance of the G20 as a hub and catalyst for the repoliticization of global economic governance during the GFC. This process was augmented by a crisis effect that undermined the cognitive authority of formerly authoritative actors and networks, thus repoliticizing conventional wisdom or background knowledge. The third explicated how G20 governance networks contested policy norms and practices in key aspects of global economic governance, influenced by decentralizing authority. The final section argued that there are important political and normative consequences from the G20's inclusivity practices, influencing the G20 and broader contexts of global governance, including, potentially, domestic politics and governance.

This analysis emphasizes the growing significance of the new G20 politics of global economic governance. This forum and its policy debates are *political*, especially because of its key contribution to repoliticizing global economic governance. The latter occurred despite pre-GFC attempts to depoliticize economic liberalization and the Washington Consensus. The

present article explicates these new political practices and networked processes of G20 governance, including their influence on global governance in the context of decentralizing strategic, political and cognitive authority.

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# Globalization 4.0 and New Modes of International Cooperation

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## Abstract

*Since the late 19th century, the international scene has witnessed several waves of globalization that have transformed regulation and cooperation between nations. The current wave — that economists have defined as “globalization 4.0” — is shaped by an industrial revolution that combines digital, physical and biological transformations. Digital technology has a deep structural impact on public and private goods such as health, education, transportation or energy, which changes the terms of the global condition. It disrupts both the organization of societies and the relation between individuals and globalization. Compared to previous waves of globalization, globalization 4.0 affects the international system and runs throughout the global social fabric by increasing throughout the world the level of inequalities and by triggering subsequent polarization and fragmentation. In this global context, our current modes of cooperation and regulation are facing growing issues of legitimacy and efficiency, that are not entirely new, but that are now becoming particularly acute. Those issues of legitimacy and efficiency are furthermore complicated by a shared experience of disconnection from globalization — the rise of the globalization’s so-called “left-behinds” — that could be characterized as a form of anomy at the international level. This complex challenge has not yet been fully embraced by the major institutions of global governance. There have been however responses at the sub-global level: connectivity politics, launched by China and followed by the European Union, is one illustration of the new paths that might be taken by global policy makers.*

**Key words:** globalization waves; Globalization 4.0; Inequalities; Connectivity politics

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## Introduction

The 2019 World Economic Forum (WEF) in Davos witnessed the emergence of the notion of “globalization 4.0” which is now slowly spreading into academic debates, albeit predominantly in the field of digital studies. It could however also prove useful to illuminate recent trends in global governance and international cooperation, and to address some of the most pressing puzzles that both International Relations (IR) scholars and policy thinkers are confronted with. According to the WEF’s white paper published a few months after the 2019 Davos summit, assessing “globalization 4.0” is a mean to understand “how profoundly the context for governance and cooperation is changing due to the Fourth Industrial Revolution” [WEF, 2019, p. 5]. This “Fourth Industrial Revolution” — an expression that was likewise generated by the WEF’s conceptual output [Schwab, 2016] — derives from the convergence of digital, physical and biological transformations, whereas the Third Industrial Revolution was essentially the widening access to digital technology. Its dynamics constitute a revolution in a deeper sense with a more

disruptive impact on the organization of societies and on the relation between individuals and globalization. This disruption defines “globalization 4.0”: it is also what economist Richard Baldwin calls “the globotics upheaval” [Baldwin, 2019], i.e. the profound impact of digital technology on public and private goods such as health, education, transportation or energy, that changes the terms of the global condition. This transformation is further complicated by, and partly responsible for, environmental crises and geopolitical shifts. Despite calls for “de-globalization” [Bello, 2002] and nativist entrenchment trends, globalization is not disappearing but, rather, radically evolving. The new globalization entails novel modes of governance and cooperation, and therefore challenges the existing order of international relations.

As its name indicates “globalization 4.0” is not the first global wave that has redefined relations between states and societies at a world level. International economists such as Richard Baldwin and Philippe Martin [Baldwin, Martin, 1999] have provided a framework of analysis that makes sense of the major global waves witnessed by human communities in a historical perspective. Although the exact starting and ending points of those different waves are hard to define, there is a general understanding of their chronological development. The first wave of globalization started in the late 19th century and was triggered by the transportation and communication revolution – the advancement of steam and coal transport engineering, the invention of long-distance communication tools – that led segments of societies around the world to experience both the perception and the reality of time-space compression on an unprecedented scale. It called for novel means of regulation that materialized into pioneer governance institutions such as the International Telegraph Union, the International Association of Railway Congress or the International Sanitary Convention, the ancestor of the World Health Organization. That first wave ended around 1914, with the breakout of the Great War and the decrease of transnational flows of goods and people. Globalization 2.0 started around the end of the Second World War when the major international organizations that still regulate relations at a planet-level today were conceived and eventually established, i.e. the Bretton Woods system and beyond. Technical innovation was also a factor in the shaping of the new regulation architecture, as illustrated by the creation of the International Atomic Energy Agency. The liberal push of the 1980s and the general lowering of barriers that accompanied the end of the U.S./USSR confrontation, soon amplified by the emergence of the “world wide web,” brought about globalization 3.0. It revived the legitimacy and power of global institutions such as the United Nations and its agencies, but it also activated other cooperation arrangements and in particular regional groupings such as the Asia Pacific Economic Cooperation (APEC) or the Mercosur, as well as global clubs such as the G20. Each wave of globalization since the late 19th century has been a mixture of technological transformations and geopolitical shifts, and each have called for global institutional change. In that sense globalization 4.0 is not essentially different from previous waves, but it does generate unique challenges. Confronted with rising level of inequalities and subsequent polarization and fragmentation, our current modes of cooperation and regulation face growing issues of legitimacy, efficiency and anomy.

## The Challenges

The challenges that are part and parcel of globalization 4.0 need to be analyzed both in the present context of global change, as well as in a historical perspective. The WEF makes a call for a new global architecture that is set against the background of the ongoing transformation of the international scene and the arguments for its case are made accordingly. Yet those arguments, such as the need for more inclusiveness and effectiveness, point to questions that have been regularly raised almost ever since the international institutions inherited from the post-1945 period were established. What makes those questions and related challenges particularly topical

in the context of globalization 4.0 is the specific blend of geopolitical transformation and technological revolution that characterizes the present wave.

## Legitimacy

There is little doubt that more than a few major international organizations are, in one way or another, in crisis: among others, NATO, according to French president Emmanuel Macron, is experiencing “brain death,” whereas the WTO, for a number of analysts, actually “died” [Adlen, 2018]. Globalization 4.0 is, at this early stage and for the time being, a development that is characterized by fragmentation and disruption rather than restructuring and re-ordering. The disruptive capacity of U.S. president Donald Trump has impacted cooperation arrangements and institutions to the point of calling into question their rationale – as, for most of them, the commitment of the world’s biggest power has been pivotal – and therefore their very existence.

Doubts about the *raison d’être* or, when expressed in more political terms, about the legitimacy of the global architecture, are not new. But the concerns have been expressed, until now, in terms of representativeness. Explaining the need for a BRIC summit, when it was launched at Yekaterinburg in 2009, Russian president Dimitri Medvedev remarked: “none of us took part in establishing the international financial system back in the 1930s–40s. I mean, none of our countries took part. Everything was decided for us. We cannot accept this situation again. We need to ensure that our countries, which between them are home to billions of people, take part in setting the new rules of the game” [President of the Russian Federation, 2009]. The demand for more inclusive, and indeed legitimate, modes of cooperation was also at the root of the rise of the South on the international scene in the decades after the Second World War, following the decolonization movement. The largest group representing developing countries, the G77, was established in 1964, in the wake of the first United Nations Conference on Trade and Development (UNCTAD).

Despite the diversity of situations now and then, there has been a recurrent dissatisfaction with the membership of the core entities of the international cooperation system. But the existence of the system itself, sustained by a notion of international community, has not been questioned. The fact that the key architect of the post-1945 cooperation system, the United States, challenges its relevance opens up a complex debate. For a number of global stakeholders it is an invitation to question the legitimacy of the liberal international order whose dominance was more or less taken for granted after 1989.

## Efficiency

Legitimacy and efficiency are strongly interlinked in the perception of international organizations, and this interlinkage plays out more than ever in the dynamics of globalization 4.0. The relative lack of legitimacy that, supposedly, affects informal governance entities such as the G20, has generally been counterbalanced by the efficiency, real or perceived, of the said entities. Conversely, the tolerance for the limits of the efficiency of an institution such as the United Nations has derived from the common perception that its essential legitimacy was hardly debatable, at least until the recent push against multilateralism. The legitimacy/efficiency nexus constitutes a sort of established paradigm well captured by the UN General Assembly (UNGA) president in 2011: “Traditional multilateral institutions, like the UN and the Bretton Woods institutions, are increasingly criticized for not being efficient and representative enough. As a response, new actors, like the G20 and other ad hoc informal groups have emerged. (...) There is a risk for the UN to be marginalized. Suffice it to recall here that when Heads of State and

government of the G20 met in Pittsburgh, on 24–25 September 2009, to work out a collective response to the economic and financial crisis, the General Debate was still going on at the United Nations in New York!” [ECLAC, 2011].

This paradigm and more specifically the tension between the “legitimacy” argument and the “efficiency” one, have been resolved over time by the regular assessment of groupings such as the G20’s output – the pioneer work of the G20 Research Group has been crucial to that effect [Kirton, 2013] – and on the other hand the yearly acknowledgment of the irreplaceable function of an international covenant such as the one provided by the UNGA. Although president Donald Trump has been attending the General Assembly meetings, as well as the G7 and G20 summits, and using them for presenting his worldviews and international policies, he has also expressed the strongest scepticism towards global cooperation since the early 20th century American isolationism. The paradox of a liberal international order whose champion is retreating then brings up the question of the capacity of an engine whose motor is running out of steam. One should note however that the shift in the U.S. attitude towards cooperation reflects a far much larger trend of national retrenchments or, at best, regional realignments. They have made the promotion of any global agenda – from nuclear deterrence to combatting climate change – more challenging.

## Anomy

The disruptive dimension of globalization 4.0 affects the international system and runs throughout the global social fabric. The year 2019 has witnessed numerous movements of social unrest around the world that, even though they occurred in different contexts, share similar expressions of doubt toward the ability of established institutions to deliver material and moral progress. Sociologist Emile Durkheim defined “anomie” as the condition of a society whose internal contract is disintegrating due to the weakening of common norms and values [Durkheim, 1893]. Translated into IR terms, anomy today is the disconnection from globalization, expressed in multiple ways. It is also what commentators have called the rise of the globalization’s “left-behinds,” which was spectacularly illustrated by the decision of the British people to leave the European Union and the social polarization that this decision revealed. Beyond and before the *Brexit* moment, however, signs of disconnection were visible in many societies. The WEF’s white paper mentioned above argues for the need of a new social contract by noting that while the digital revolution has decisively contributed to the rise of living standards and to the reduction of poverty, there has been “systematic underappreciation of the human impact of rapid economic change, whether due to technology or policy liberalization, in the priorities of national economic policy and the corresponding international institutional architecture” [WEF, 2019, p. 26].

The challenge of anomy is a new element in the recurring debates about the relevance of the international architecture inherited from the post-1945 order. On the positive side, this novelty reflects the emergence of a form of people’s empowerment on a new scale, a global “voice” as economist Albert Hirschman would put it [Hirschman, 1970]. But following Hirschman’s paradigm of “exit, voice and loyalty” there is a risk of large scale “exit” as well, in the shape of growing resentment and distrust of governments and intermediary bodies.

## Responses

Even before the appearance of the term globalization 4.0, there were signs of a general realization that with the fourth industrial revolution came unforeseen challenges requiring new modes

of cooperation. For example, the transition, in 2015, from the UN's Millennium Development Goals (MDGs) to the Sustainable Development Goals (SDGs) pointed to the fact that the previous third industrial revolution had markedly boosted economic development, to the point of blurring the clear-cut North/South division – with a majority of the poorest people living in middle-income countries – calling for new approaches to the question of redistribution of global wealth. The growing presence, and visibility, of the globalization's "left-behinds" in both developing and developed societies uncovers issues that are complex and as such have not yet been embraced by the major institutions of global governance. There have been however responses at the sub-global level: the most articulated and far-reaching one has been so far that of China with its "One Belt One Road" (OBOR), later re-branded "Belt and Road Initiative" (BRI). Turning globalization 4.0 on its head, Chinese policy thinkers have presented the new global wave as an opportunity and a turning point in the evolution of world order and modes of cooperation. The Chinese approach to solving the unbalances of globalization, and more specifically its connectivity politics, has triggered other, similar responses, from Asia and Europe. Meanwhile, and as demonstrated during the 2019 summits of the G7 and the G20, there is a now a clearer recognition of the need for re-centring people and people's inclusiveness within the global agenda designing process.

## Connectivity

Looking at globalization 4.0 as a process through which global governance practices are redefined is opening new and potentially fruitful debates within the public policy epistemic community. It has also renewed the conversation on "globalization with Chinese characteristics" [Henderson, Appelbaum, Ho, 2013]. According to Jia Wenshan and Jiang Haofeng, the definition of "globalization 4.0" sustained by the fourth industrial revolution, is too narrowly focused on technology but should also take into account other dimensions of the structural crisis that accompanies the fourth global wave. For those two authors the term "globalization 4.0" as it was used at the 2019 Davos Forum is "another name for Industry 4.0, downplaying or even ignoring the fact that globalization should be an all-encompassing and grander narrative covering politics, economics, culture, science and technology" [Jia, Jiang, 2019]. Seen from this perspective, globalization with Chinese characteristics appears as a civilizational approach to the challenges of the fourth global wave, and has indeed been an important component of Beijing's narrative on the Belt and Road Initiative, also called the "New Silk Road." In practical terms, the civilizational approach has been implemented through a proactive promotion of connectedness or "connectivity politics" [Kohlenberg, Godehardt, 2018]. The gigantic set of projects encompassed by the BRI aims at connecting regions, countries and people with steel and concrete infrastructures, digital networks and more generally with tools that facilitate flows both domestically and internationally. Its focus on the "left-behinds" of globalization, first within China, in the Western and Central provinces, and then beyond it, in Central Asia and Africa, echoed with the global concern with growing inequalities.

Connectivity politics is therefore not only about connecting societies and communities but also about reconnecting entities that have been fragmented by the dynamics of rapid growth under the digital revolution, as the divide between those who have benefited from the global third industrial wave and those who were left behind, more than often crosses through countries – such as China or other emerging powers – that were on average less developed but somewhat more cohesive. In that sense the connectivity politics that inform the conception and implementation of the BRI is a response to the inclusiveness issues brought about by globalization 4.0. For Wang Huiyao, the ongoing multilateralization of the BRI, bringing in a growing

number of stakeholders that makes it increasingly open and inclusive, gives this mega-project the potential to “work as a vector for globalization 4.0” [Wang, 2019].

The BRI is however still a work-in-progress; its development has not been without issues and has generated questions about transparency, accountability, and long-term viability, among others [Lindberg, Lahiri, 2018]. Yet it has also triggered emulation. The European Union and Japan have been drafting their own respective connectivity politics, and have as well signed in September 2019 the “EU-Japan Partnership on Sustainable Connectivity and Quality Infrastructure.” This partnership, as its name indicates, aims at redefining the terms of connectivity politics by introducing a more normative content with sustainability and quality standards inspired by the UN’s ambitious SDG program. This, in turn, has arguably had an impact on the official BRI’s narrative. The concern for environmentally responsible and high-quality projects is now far more visible than it was in the early days of the OBOR. In his speech at the 2019 Belt and Road Forum, Chinese president Xi Jinping stressed that the Chinese initiative would “protect the common home we live” by building “high-quality, sustainable, risk-resistant, reasonably priced, and inclusive infrastructure” [Ministry of Foreign Affairs of the People’s Republic of China, 2019].

## Empowerment

Connectivity politics might, in the longer term, contribute to the shaping of the new international architecture that the WEF is advocating for, but it is not, however, a direct response to the institutional issues put forward by the Davos Forum community. For the time being, connectivity initiatives offer solutions to the efficiency issues of globalization 4.0, and more specifically to the need for better distribution of wealth and inclusiveness within the new dynamics of the fourth industrial revolution. The implementation of such initiatives can differ from country to country and has not produced a unified global set of norms and practices. Projects and partnerships formed under the label of connectivity often converge towards similar goals that, added to each other, constitute a loose common agenda, such as the protection of “our common home,” as president Xi Jinping put it. But as a policy paper by S. Grimm and S. Weinlich of the German Development Institute stresses, a tacit or even explicit consensus on the definition of a global common good is only a preliminary condition for the establishment of a solid international co-operation system and does not either guarantee the stability of such a system: the future of the multilateral system that was conceived during the 20th century is therefore uncertain [Grimm, Weinlich, 2020].

The weakening of multilateralism tends to be associated with the rise of populism, an association that seems, again, to be perfectly illustrated by American isolationism and the election of Donald Trump. Yet as Pierre Rosanvallon notes, one should distinguish the theatrics through which populism expresses a mood of disillusionment – with some real policy consequences – from what actually feeds it. What is called populism is also a diversity of manifestations revealing a widespread expectation of a renewed social contract involving a stronger, more empowered civil society [Rosanvallon, 2019]. Without a larger and systematic acknowledgment of this expectation, the reconnection of “left-behind” people and communities with global development might prove difficult. But to be efficient such an acknowledgement cannot be confined to a domestic periphery or be an addition of national assessments. It has to be global in order to encompass the scope of the unevenness of globalization 4.0, and the broad phenomena of disruption and fragmentation that go with it. Both the 2019 Osaka G20 summit and the Biarritz G7 summit have given central stage to the issue of global inequalities. At the Biarritz gathering French president Emmanuel Macron underlined the importance of a rules-based international

cooperation system as a “powerful tool to fight inequalities” [G7, 2019]. From that perspective it is not the principle of the current cooperation system – the assemblage of multilateral tools – that needs to be revisited but its purpose.

Addressing the challenges of globalization 4.0 is evidently a multidimensional ambition for which there is no predefined roadmap. The limits of the modes of cooperation inherited from the post-Second World War, even with its successive amendments, engender a combination of issues of efficiency, legitimacy and anomy that seem to have reached a tipping point. The post-1945 international architecture came with a normative package – shaped by Western liberalism but also by some of the counterpoints brought about by the decolonization movement and the Global South perspective – a repertoire of international norms that is now partly unravelling. New international norms might need to be defined in order to reset the global institutional framework of cooperation. The connectivity politics of China, Japan and the European Union, and their convergence toward the idea of “sustainable connectivity,” indicate that the response to the problem of fragmentation characterizing globalization 4.0 cannot be a strictly technical, “value-free,” one: normative choices seem inevitable. Making those choices will most probably entail a global battle of ideas and influence but, as again the example of connectivity politics within the Asia-Europe space shows, this battle will not necessarily lead to more division and can actually produce some new normative basis for international cooperation.

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# Explaining BRICS Outreach: Motivations and Institutionalization

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## Abstract

*This article examines and explains the outreach activity of the BRICS group of Brazil, Russia, India, China and South Africa. We focus on two research puzzles: a) the motivations and b) the form and degree of the institutionalization of BRICS outreach. We define outreach as collaborative interaction among BRICS and other actors within and outside the BRICS area and focus on outreach to governments of non-BRICS countries and national top officials representing regional organizations. First, we offer a theoretical framework based on the experiences of the Group of 7/8 (G7/8) and the Group of 20 (G20), considering both commonalities and differences with BRICS. Second, we provide a detailed empirical analysis of BRICS outreach over time. Third, we explain BRICS outreach in light of the theoretical framework and enrich it based on our findings. Methodologically, we draw empirical information from official documents, news media and academic literature. We argue that the outreach activity of a major power grouping is reflective of its internal cohesion, as well as of how it defines its own position in the world and how it is perceived by others. This research offers a timely contribution to the ongoing debate on BRICS and the under-researched BRICS outreach process as a part of the overall institutionalization of BRICS.*

**Key words:** BRICS; outreach; BRICS Plus; Gx; motivation; institutionalization

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## Introduction

Over the past decade, we have witnessed the development of BRICS as a major power grouping. Along with the deepening of the institutionalization of BRICS, the BRICS outreach concepts and practices are also gradually taking shape. Outreach towards the rest of world is related with two larger dimensions: how BRICS defines its role in global governance and how it gets institutionalized as an organization. Several scholars have already studied the interaction among BRICS and the wider geopolitical and multilateral system [Dijkhuizen, Onderco, 2019; Duggan, 2015; Shelepov, 2018]. Others have investigated the growth and institutional development of BRICS as such [Cooper, 2016; Kirton, 2015; Larionova, Shelepov, 2015; Stuenkel, 2015]. However, the why and how of BRICS outreach remain under-researched.

BRICS outreach can be defined as collaborative interaction among the BRICS actors (governments and institutions) and other actors within and outside the BRICS area, such as other governments, multilateral institutions, business and civil society. For the purpose of this

paper, we focus on outreach to governments of non-BRICS countries and national top officials representing regional organizations. We leave out non-governmental actors and secretariats of multilateral organizations as this would amount to different research questions and theoretical implications.

Our research addresses two interrelated questions: 1) the motivations of the BRICS grouping for its outreach activity, and 2) the form and degree of institutionalization of the BRICS outreach. In the remainder of this paper, we offer a theoretical framework based on the experiences of the G7/G8 and the G20, considering both commonalities and differences with BRICS. As we will argue, the outreach activity of a major power grouping is reflective of its internal cohesion, as well as how it defines its own position in the world and how it is perceived by others. After presenting the theoretical framework, we provide a detailed empirical analysis of BRICS outreach. Next, we explain BRICS outreach in light of the theoretical framework, and enrich it based on our findings. Methodologically, we draw our empirical information from official documents, news media and academic literature.

## Gx Outreach Practices and Theoretical Framework

In order to construct a theoretical framework to understand BRICS outreach, we draw inspiration from other major power groupings, namely the G7/G8 and G20 (the Gx groupings), whose outreach activities have a slightly longer history. After we have build-up the theoretical framework, we will apply it to the BRICS outreach and look for both commonalities and differences.

### ***The Motivations of Gx Outreach***

An initial fundamental question we have to ask is why a relatively small major power grouping would want to cooperate with non-member countries. Part of the purpose of the group relates to functions that can be fulfilled among the members themselves: coordinating macro-economic policy, energy, environmental and other policies; coordinating diplomatic positions vis-à-vis the rest of the world; or peer learning. If the group cooperates directly with other countries, such activity requires specific explanation. It is a way to have an impact on those non-members, which can take several forms.

### ***Group Hegemony***

A useful concept, offered by the Canadian scholar Allison Bailin, to make sense of the outreach activity of the G7/G8 and G20, is “group hegemony.” This concept, which was originally based on the G7 case, implies that the group as such undertakes a bid for hegemony in the global economy. The theory of group hegemony draws from hegemonic stability theory. In contrast to the latter, the former holds that the hegemonic function of keeping the global economy stable by providing global public goods and multilateral regimes is no longer assumed by a predominant great power alone, but by a group of powerful countries. This group (c.q. the G7) has taken over the role of a declining great power (c.q. the US), and is characterized by a concentration of economic power, a group identity and a commitment to economic liberalism [Bailin, 2005]. This theory resonates with what Keohane already observed in the early 1980s. With the single hegemonic power in decline, the underwriting of the multilateral system can be taken over by an “oligopoly,” c.q. the G7 summits at that time [Keohane, 1984].

The concentration of power allows the group hegemon to provide for global public goods such as liquidity and the ability to act as the lender of last resort, large and wealthy consumer markets, foreign direct investment, and security functions. Literature on international coopera-

tion maintains that the group should not be too small or too large. When it is too small, it cannot provide public goods. If it is too large, it faces high transaction costs and is unable to manage defection. In a group with the right size – the designate k-group – the members realize that the international public goods can only be achieved if all members contribute. Group identity adds to this commitment and the strong pressure not to defect. As powerful and competitive economies, the group members are keen to export and invest overseas. Hence they have a large stake in global financial-economic openness and stability [Bailin, 2005; Lake, 1993].

Bailin did not touch upon direct outreach to non-member countries, but does include G7 political control over multilateral institutions such as the International Monetary Fund (IMF) and World Bank Group (WBG) [Bailin, 2005]. Through this kind of institutional power [Barnett, Duvall, 2005], non-members are influenced in an indirect way. Still, direct outreach can be understood as bolstering group hegemony, more precisely by increasing group capacity, raising group legitimacy, and socialization of non-members into group visions (see below).

The theory is, besides the G7/G8 and BRICS, also applicable to the G20, including with regard to the outreach dimension. The G20 was created at finance ministers' and central bankers' level in 1999 in the wake of the Asian financial crisis and elevated to leaders' level at the zenith of the global financial crisis. The G7 had obviously become too small to fulfill the function of group hegemony in a world in which large emerging economies played key roles in international financial crises both as origins and solutions. However, a weakness of the G20 is the much lesser developed group identity.

In sum, the theory of group hegemony offers a theoretical framework to understand the creation and continuity of the G7/G8 and G20 and their role in the world economy and world politics. Their outreach to non-members supports this role. The question is to what extent this theory is applicable to the BRICS. In terms of economic power concentration the BRICS is far from being in a position to assume hegemony in the form of a "designate k-group." It has never displayed, let alone expressed such an ambition, unlike the pre-Asian-crisis-G7/8, which also used its outreach for this purpose (see below). However, most BRICS members have more and more interests abroad, and to support these interests, they are more and more active overseas. It would be logical if they used their collective BRICS platform for this purpose as well. As such, "group hegemony" can be seen as the advanced stage of a process, starting with the group's first steps to influence the global political economy in light of its own interests. Furthermore, another parallel between G7/8 and BRICS comes to mind. The G7 was created to complement the capabilities of the US as the *declining* hegemon. In a sense, we could argue that the BRICS complements the capabilities of the preponderant power in the BRICS, namely a *rising* China, that similar to the US, has an increasing stake in the course of the world economy and world order, and might be willing to instrumentalize the BRICS platform.

### *Group Effectiveness Through More Capacity*

One motivation of direct outreach is to enhance the effectiveness of the group by bringing on board the capabilities of non-members for joint action. In the G7, after Canada and the EU became members in 1976 and 1977 respectively, we saw outreach to the Soviet Union and Russia in the 1990s, culminating in Russia's full-fledged membership in 1998 [Kirton, 2015].

The outreach partners contribute to the group's goals with their resources or with domestic reforms. With more participants come more capabilities. For the G8 in order to be able to meet its ambitions as a steering group for global governance, it had to bring in the loop countries such as the G5 (China, India, Brazil, Mexico, South Africa), whose policies have major impacts on the global economy, climate change or African development [Shaw et al., 2008]. At its summit in Evian (2003), the G8 decided to create the Africa Partnership Forum, which included

11 other Organization for Economic Cooperation and Development (OECD) donor countries and African representatives [Blake, 2012]. Sometimes, it is primarily a matter of money: in 2010, the non-members Netherlands, New Zealand, Norway, Republic of Korea and Switzerland joined the G8 Muskoka Initiative pledging money to boost the Millennium Development Goals (MDGs) on maternal, newborn and child health [Bhuskan, Slahub, 2014]. For the time being, the capacity motive is less present in G20 outreach to other countries. This Gx experience leads us to a first hypothesis with regard to a materially driven motivation for outreach.

**HYPOTHESIS 1:** BRICS reaches out to non-member countries to increase its effectiveness in achieving its policy goals.

### *Group Legitimacy*

Whereas the first motivation is driven materially, the next three are of a constitutive nature, i.e. aimed at shaping political positions, worldviews and identities of non-member countries. Both the G7/G8 and G20 have met contestation based on legitimacy grounds. The main reason is that they openly assumed a leadership role in global governance in general and thus affected the interests of non-member countries. The G7/G8 had gradually been expanding its agenda, and involving multilateral institutions such as the IMF, WBG and OECD, which are dominated by the G7/G8, but include many non-members. With its political clout and resources the G7/G8 has also played an essential role in areas such as post-Soviet transition, the Asian financial crisis, and African development. The G20, in its turn, has led the response to the global financial crisis from its first 2008 leaders' summit onwards, by coordinating the national policies of 19 major economies plus the EU and tasking an array of international financial institutions. Inviting other countries to summits and other meetings, is a way to raise legitimacy through a) involving non-members in Gx decision-making, as well as b) allowing those leaders to enjoy the prestige vis-à-vis domestic and international audiences of participating in such powerful clubs.

From the 2000s onwards, the G8 realized it had to address this "crisis of legitimacy" [Shaw et al., 2008]. In 2000, Japan was the first G8 chair to invite African leaders to its summit in Okinawa [Cornelissen, 2012]. Since then until now, the G8 has always invited leaders of African countries to its summits (with an interruption in 2013 and 2014). At the 2003 Evian summit, France also invited the leaders of the rising powers China, India, Brazil, South Africa and Mexico. From 2005 until 2009, these so-called Outreach 5 (O5) or G5 leaders joined each G8 summit. However, the G8+5 format ceased to exist in 2009, when the G20 decided to continue as an annual leaders' summit [Kirton, 2015].

The birth of G20 summits changed the identity of the G8. The exit of Russia over the Ukraine crisis in 2014 reinforced the identity of the renewed G7 going back to its roots as the caucus of the major Western powers in a tense world. This evolution lowered the global governance ambitions of the G8, and concomitantly, the need to build-up legitimacy in the rest of the world. Still, in 2019, G7 chair France again invited India's prime minister, as an ad hoc initiative along with African and other leaders. This reflects a practice over the past 16 years of randomly inviting non-member countries, in addition to the now defunct G5 and ongoing Africa outreach.

The G20 has also developed an outreach practice to non-member countries. From the first summit in 2008 on, Spain has been invited as a "permanent guest." The prime minister of Netherlands has been invited several times, including in all summits since 2017. In addition, the G20 also invites the chairing countries of regional organizations, notably the African Union, NEPAD, ASEAN, and, irregularly, APEC and CARICOM. Already in 2009, the G20 got contested by a number of countries, including financial centers that disagreed with the G20-OECD

initiative at the London summit to list jurisdictions as non-cooperative tax havens. In response, Singapore convened the 30-member Global Governance Group (3G), which included other financial centers, such as Switzerland, along with a few other industrialized and developing countries. From the 2010 Seoul summit onwards, a 3G country – mostly Singapore – has always been present [Cooper, Momani, 2014; Luckhurst, 2016]. Hence, we can formulate a second hypothesis concerning outreach motivation:

**HYPOTHESIS 2:** BRICS reaches out to non-member countries to enhance its international legitimacy.

### *Socialization of Non-Members into the Group Vision*

Outreach can be a group strategy to influence non-members, more precisely to reshape their governments' policies, views, and interests by socializing them into the group's consensus in terms of common interests and views. According to experts as well as outreach country officials, this intention was present in both the G8 outreach to Africa and to the G5 [Nafey, 2008; Woodward, 2008].

In July 2000, in the margins of the G8 Okinawa summit, the leaders of Algeria, Nigeria and South Africa met with the G8 leaders. Those three stood at the forefront of the call for a new African development strategy, which would resonate with the post-Washington Consensus or "Third Way" mindset of the G8 leaders at that time [Black, 2012; Cornelissen, 2012; G8, 2000]. In 2000–01, the governments of Algeria, Egypt, Nigeria, Senegal and South Africa promoted initiatives for African economic development that merged into the New Partnership for African Development (NEPAD). NEPAD was adopted by the Organization for African Unity (OAU, which turned into the African Union in 2002) in July 2001. The same month, in the presence of the leaders of Algeria, Mali, Nigeria and South Africa, it was endorsed by the G8 summit in Genoa [G8, 2001]. The joint G8 and NEPAD agendas revolved around the idea of Africa's own responsibility and a post-Washington Consensus vision including good governance, pro-market reforms, trade liberalization, as well as security, social development, water and agriculture. Although the new agenda for Africa partly originated from a few African governments themselves, G8 donors were always closely involved, and tried to consolidate their influence through endorsing activity [Black, 2012; Cornelissen, 2012; Engel, 2012; Taylor, 2012].

In the outreach effort to the G5, notably the Heilighendamm Process (HP) (2007–09), the agenda was unilaterally set by the G8 and largely reflected Western priorities [Leininger, 2009]. It included a) promoting cross-border investment, including corporate social responsibility, b) promoting research and innovation, including the protection of intellectual property rights, c) fighting climate change, according to the principle of common but differentiated responsibilities and respective capabilities, d) cooperation on clean and renewable energy, and e) development, particularly in Africa [G8, 2007]. By opening profound dialogue on these topics, the G8 most likely aimed at socializing the G5 in its views and approaches. This strategy was strengthened by letting the OECD coordinate the process. The OECD is specialized in soft forms of governance that include peer-learning and sharing of best practices, often at technocratic levels. This offers a conducive environment for socialization. Woodward also points at the socialization potential and motive in involving the OECD in the HP: "Deeper participation in a body such as the OECD could have important socialization effects for the O5 countries exposing them, and possibly making them more amenable, to the norms of behavior in the OECD-G7/8 world" [Woodward, 2008, pp. 274–5]. The above analysis brings us to another hypothesis:

**HYPOTHESIS 3:** The BRICS reaches out to non-member countries to socialize them into shared BRICS views.

### *Instrumentalization of Group Outreach by Individual Group Members*

Adding non-members' capacities, increasing legitimacy and socialization of outreach partners as material and constitutive forms of interaction all help to consolidate group hegemony. However, outreach can also serve individual members' particularistic purposes. Individual group members might instrumentalize the group to advance their particular interests in relation to non-member countries. This motivation is different from the third when these individual interests are independent of the group consensus. In this case, that member utilizes the group as a power multiplier, since the other members' hard and soft power capabilities are added to one's own.

In the G8 and G20, we only see a soft form of this motivation. In these bodies, the rotating chairs in particular as hosts of the summits possess an important amount of decision-making power over the outreach process during their presidency. Rotating chairs often invite non-members to beef up their bilateral ties. The invitees are often regional partners. For example, Japan (2008, 2016) and Canada (2010, 2018) invited respectively Asian-Pacific and American countries to their summits. G20 chairs sometimes invite regional partners, for example New Zealand at the 2015 Brisbane summit in Australia, Azerbaijan at the 2015 Antalya summit in Turkey, or Vietnam at the 2019 Osaka summit in Japan. Hence we can formulate a final hypothesis on motivation:

**HYPOTHESIS 4:** The BRICS reaches out to non-member countries for material or constitutive reasons upon the initiative of individual BRICS members in function of their individual interests.

### ***The Form and Degree of Outreach Institutionalization***

Institutionalization pertains to the questions of how the group organizes the outreach over time and to what extent continuity and consistency are achieved in involving non-members. Weak institutionalization would be characterized by a lack of organizational arrangements to sustain outreach over a longer term and quite irregular patterns of selecting and involving non-members. Strong institutionalization would be reflected in a serious organizational investment and stability of the patterns of outreach partners and activities. In sum, institutionalization rests on organization, consistency and longevity. Again, the Gx outreach experiences provide inspiration for theorizing.

The G8-Africa cooperation, or "Africa Outreach," got institutionalized quite rapidly. In Genoa in 2001, the G8 leaders decided to appoint personal representatives for Africa [Black, 2012]. In Evian in 2003, the G8 created the Africa Partnership Forum, which included 11 other OECD donor countries and African representatives. Even though there was never a fixed Africa outreach group, the leaders of Algeria, Egypt, Nigeria, Senegal and South Africa (who were invited several times) and others (in varying combinations), as well as the head of the African Union, were invited to most subsequent G8/G7 summits until the present. African development was there to stay on the G8 agenda, and often subject to comprehensive G8 plans. This relatively solid institutionalization can be linked to the G8 members' quite coherent post-Washington Consensus or "Third Way" mindset at that time (see 2.1.4).

The G8 was internally divided on the G8+5 format and the corresponding Heiligendamm Process. The UK, France and Germany were enthusiastic about this approach in order to enhance the legitimacy and impact of the G8. French and British leaders had already expressed their support for a full-fledged expansion to the G8. But the US were skeptical. For example they had not invited the G5 to their 2004 Sea Island summit [Shaw et al., 2008, p. 33]. The Bush administration tended to consider the G8+5 forum as a redundant talk-shop that undermined

the value of intimate conversations among a small number of Western leaders. Japan and Canada, as non-members of the permanent group in the UN Security Council, were wary of seeing their relative weight diluted in a wider format, including Japan's Asian competitor China [Kirtton, 2008]. These observations lead us to the first hypothesis concerning institutionalization:

**HYPOTHESIS 5:** Political cohesion within the group with regard to the outreach strategy leads to strong institutionalization. Consensus on the outreach strategy in its turn can be influenced by the overall political cohesion within the group.

We assume that outreach institutionalization partly depends on the attitudes of the outreach partners themselves. They should not be considered as passive players vis-à-vis the major power group's advances. In the case of the G8 Heiligendamm Process, it became known that some of the G5 partners were uncomfortable with the G8 dominance in the agenda-setting and procedure. The agenda was unilaterally set by the German chair and the G8, without consultation with the G5. G5 agenda suggestions were ignored. There was also unease about the role of the OECD that was tasked by the G8 to facilitate the process. China, India, Brazil and South Africa are not members of the OECD, which in the Global South is often regarded as a "rich men's club" [Cooper, 2008, pp. 14–5; Leininger, 2009; Nafey, 2008]. The specific problem here is that the G8 was engaging with other major powers, which self-identify as equals in a still asymmetrical format. In the new G20 summitry, the former G5 partners had at least a sense of full ownership as full members, rendering the G8+5 format immediately redundant. Probably, the G8+5 would have disappeared rather sooner than later even without the G20 summits. Outreach to smaller countries, in contrast, is very different, as they tend to accept the asymmetry of the relationship, and might be content to be invited to a quite prestigious table. In addition, as was visible in the G8 Africa outreach, some key African partners actively sought G8 support for their NEPAD initiative. This inspires a second hypothesis:

**HYPOTHESIS 6:** Institutionalization of outreach with major powers is hard to sustain without full ownership over the process. Smaller powers are more tolerant towards power asymmetry.

*Table 1.* Theoretical Framework and Hypotheses

Explanandum	Theories & Perspectives	Hypotheses
Motivations of Gx outreach	Group effectiveness through more capacity	HYP1: BRICS reaches out to non-member countries to increase its effectiveness in achieving its policy goals
	Group legitimacy	HYP2: BRICS reaches out to non-member countries to enhance its international legitimacy
	Socialization of non-members into the group vision	HYP3: The BRICS reaches out to non-member countries to socialize them into shared BRICS views
	Instrumentalization of group outreach by individual group members	HYP4: The BRICS reaches out to non-member countries for material or constitutive reasons upon the initiative of individual BRICS members in function of their individual interests
The form and degree of outreach institutionalization	Political cohesion	HYP5: Political cohesion within the group with regard to the outreach strategy leads to strong institutionalization. Consensus on the outreach strategy in its turn can be influenced by the overall political cohesion within the group
	Power asymmetry	HYP6: Institutionalization of outreach with major powers is hard to sustain without full ownership over the process. Smaller powers are more tolerant towards power asymmetry

## Exploring the BRICS Outreach: Empirical Findings

### ***Situating the BRICS Outreach in the Process of BRICS Institutionalization***

The development of BRICS outreach concepts and practices should be situated in the overall process of BRICS institutionalization. Against the backdrop of the 2007–09 global financial crisis (GFC) and the reduced legitimacy of the G7/G8 in global governance, the relatively resilient BRIC countries began to enhance political cooperation through the BRIC platform and better use their temporarily increased bargaining power to be effective agenda setters [Stuenkel, 2013]. From then on, the BRICS outreach is gradually taking shape along with the development of the institutionalization of BRICS grouping as such.

At the very beginning of the BRIC cooperation in 2009, the outreach concept was not explicitly raised. The first instance of BRIC outreach can be dated back to the accession of South Africa. In 2010, the president of South Africa Jacob Zuma was invited for the first time as a guest at the BRIC Brasília Summit. In the following year under China's presidency, the Sanya Summit resulted in an important strategic decision: incorporating South Africa as its full member, adding the S to BRICS.

Although the economic power of South Africa is hardly comparable with the other four countries, its inclusion has profound political and outreach implications. Because of Johannesburg's leading role in Africa and membership in the G20 and other multilateral arrangements, it enhanced the coverage, representativeness and geopolitical influence of the BRICS as a group of rising powers. The BRICS became a unique major power grouping bringing together five different rising powers from four continents without the participation of the US or any other established power.

As stated in the 2011 Sanya Declaration, BRICS cooperation is “open to increasing engagement and cooperation with non-BRICS countries, in particular emerging and developing countries, and relevant international and regional organizations” [BRICS, 2011]. Since then, the outreach has evolved as part of the evolution of the BRICS institutionalization.

### ***One Outreach, Two Formats, Dual Channels***

From 2013 onwards, we observe that the BRICS outreach with non-BRICS countries is mainly based on two formats: the BRICS regional outreach and the BRICS Plus (also known as BRICS+). BRICS regional outreach consists of networking with the respective rotating presidency's sub-regions. Under the rotating presidency, BRICS takes its geopolitical advantage by strengthening institutional links with its sub-regions and enhancing South-South dialogue. BRICS Plus, in contrast, is not restricted to respective sub-regions but rather offers a flexible, diverse, open approach to networking with diverse partners. In addition, the BRICS outreach occurs through various channels, but is most visible through its summits and own institutions.

*Table 2.* The BRICS Outreach

BRICS outreach		Networking with non-BRICS countries, in particular emerging and developing countries, and relevant international and regional organizations	
Formats	Regional Outreach	Networking with countries and organizations in the respective rotating presidency's sub-regions	E. g. Africa Union (AU), the Union of South American Nations (UNASUR), the Community of Latin American and Caribbean States (CELAC), the Shanghai Cooperation Organization (SCO), the Eurasian Economic Union (EAEU), Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation countries (BIMSTEC)

BRICS outreach		Networking with non-BRICS countries, in particular emerging and developing countries, and relevant international and regional organizations	
<b>Formats</b>	BRICS Plus (BRICS+)	Flexible, diverse, open networking with varying countries and organizations (in varying combinations)	Egypt, Guinea, Mexico, Tajikistan, Thailand, Argentina, Indonesia, Jamaica, Turkey
<b>Channels</b>	Summits	Hosting Joint Summit, inviting partners and guests	E. g. the BRICS – Africa Outreach, Joint summit with SCO-EAEU, Joint summit with BIMSTEC
	BRICS-institution	BRICS New Development Bank	<i>Membership:</i> the NDB Agreement states it shall be open to members of the United Nations and shall be open to borrowing and non-borrowing members [BRICS, 2014b]. <i>Regional offices:</i> Africa Regional Center in Johannesburg (South Africa), Americas Regional Office in Sao Paulo (Brazil), sub-office in Brasília (Brazil), Eurasian Regional Centre Moscow (Russia). <i>Global Partnership:</i> Multilateral Development Banks (MDBs), National Development Banks, Commercial Banks, Multilaterals, Enterprises, Academia [NDB, 2020]

### *The BRICS Outreach/Plus via Summit*

#### Regional Outreach with Africa

The very first BRICS outreach practice with its regional partners started in 2013. In March 2013, South Africa hosted the 5th BRICS summit in Durban under the theme entitled “BRICS and Africa: partnerships for development, integration and industrialization.” For the first time, the BRICS leaders invited the African Union (AU) to join the summit. At the Summit, BRICS leaders agreed to establish the New Development Bank (NDB) and the BRICS Contingent Reserve Arrangement (CRA). After the Summit, a retreat was held by BRICS leaders and 15 African leaders under the theme: “Unlocking Africa’s potential: BRICS and Africa Cooperation on Infrastructure” [BRICS, 2013]. The BRICS stated in the eThekweni Declaration: “We are open to increasing our engagement and cooperation with non-BRICS countries, in particular Emerging Market and Developing Countries (EMDCs), and relevant international and regional organizations.” Consequently, BRICS regarded the retreat as “an opportunity for BRICS and African leaders to discuss how to strengthen cooperation between the BRICS countries and the African continent” [Ibid., 2013]. In the retreat, sustainable infrastructure development in Africa was deemed as critical to promoting its regional integration and industrialization and as an important area for the BRICS to support.

#### Regional Outreach with South America and Latin America

Following the same format, in July 2014, Brazil hosted the 6th BRICS Summit in Fortaleza under the theme of “Inclusive Growth: Sustainable Solutions.” Leaders of the Union of South American Nations (UNASUR) and the Community of Latin American and Caribbean States (CELAC) were invited to attend the Summit and discussed “shared interests” with BRICS leaders [Ibid., 2014c]. The BRICS leaders declared: “We renew our openness to increasing engagement with other countries, particularly developing countries and emerging market economies, as well as with international and regional organizations, with a view to fostering cooperation and solidarity in our relations with all nations and peoples” [Ibid.]. BRICS leaders believed that the strengthened dialogue among BRICS and South American countries can play an active role in enhancing multilateralism and international cooperation. Moreover,

they reiterated their commitment made during the BRICS Leaders-Africa Retreat at the 5th BRICS Summit to foster and develop BRICS – Africa cooperation in support of the socio-economic development of Africa, particularly with regard to infrastructure development and industrialization.

### Regional Outreach with Eurasia

In July 2015, under the theme of “BRICS Partnership – a Powerful Factor of Global Development,” the 7th BRICS Summit, the 15th Shanghai Cooperation Organization (SCO) Summit and the Eurasian Economic Union (EAEU) Summit were jointly held by Russia in Ufa [BRICS, 2015]. It offers an interesting prism to see how the BRICS platform and outreach linkages serve the interests and goals of BRICS member states. First, against the backdrop of the Ukraine Crisis, Russia became isolated in international affairs. It was put under EU and US sanctions, and its membership of the G8 was suspended. Hence the importance for Russia’s economic and foreign policy of the G20, BRICS, SCO, and EAEU markedly increased. The joint summit offered a multi-channel for Russia to gain support from and deepen practical cooperation with its partners (especially Russia and China in this case, so-called “Sino-Russian rapprochement”) and strengthen its international status. For instance, on 8 May 2015, two months prior to the summit, Russia and China had signed a Joint Statement on the cooperation in docking the Belt and Road Initiative (BRI) and construction of the EAEU, opening up new prospects for deepening practical cooperation among the member states of the SCO [Kremlin, 2015]. Beyond its traditional security and political focuses, the SCO started to gradually develop the dimension of economic cooperation, and its function of linking the EAEU with BRI was further discussed during the summit. After the summit, the joint SCO-BRICS Business Forum as well as the BRICS and SCO Youth Forum were held by Russia.

### Regional Outreach with South Asia and Southeast Asia

In October 2016, in order to further reach out and enrich understanding and engagement with developing and emerging economies, the BRICS – BIMSTEC Outreach Summit (BIMSTEC, Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation comprising Bangladesh, Bhutan, India, Myanmar, Nepal, Sri Lanka and Thailand) was hosted under the theme “Building Responsive, Inclusive and Collective Solutions” by India in Goa [BRICS, 2016]. BRICS regarded the Outreach Summit as an opportunity to renew friendship with BIMSTEC countries as well as to jointly explore possibilities of expanding trade and commercial ties, and investment cooperation between BRICS and BIMSTEC countries [Ibid.]. The BIMSTEC, sometimes referred to as mini SAARC (South Asian Association for Regional Cooperation), lacks regular summit record and visibility. For BIMSTEC, the outreach summit offered a superior channel to boosting ties with emerging powers and enhancing its visibility. The two groupings discussed matters of mutual interest, exchanged views on global and regional issues including the United Nations 2030 Agenda for Sustainable Development. After the Retreat, the BIMSTEC Leaders released the 2016 Retreat Outcome Document which emphasized the value of outreach in generating trust and understanding as well as promoting further cooperation among countries of the two groupings [BIMSTEC, 2016].

### Outreach with Flexible and Diverse “Plus”

Building on a similar format, facing criticisms on BRICS as an exclusive club [de Coning, 2017], and going beyond outreach with respective sub-regions, a new concept and outreach format was introduced under China’s 2017 presidency: “BRICS plus.” It was first

mooted by Chinese Foreign Minister Wang Yi at a press conference for the 5th session of the 12th National People's Congress in Beijing, March 8, 2017. Wang said BRICS would "build a new platform for south-south cooperation, exploring a "BRICS plus" format by holding dialogues with other major developing countries or groups of developing countries to establish a more extensive partnership" and "widen the circle of friends of the BRICS and turn it into the most influential platform for south-south cooperation in the world" [Xinhua, 2017]. It was defined more clearly prior to the Summit. On 30 August 2017, responding to journalists at a briefing held by the Ministry of Foreign Affairs on the 9th BRICS Summit and Dialogue between EMDCs, Wang Yi noted that the idea of the "BRICS Plus" format is "openness, inclusiveness, cooperation and mutual benefits," which is highly consistent with the BRICS spirit. The purpose of the "BRICS Plus" format is to strengthen dialogue and cooperation between BRICS countries and other EMDCs, promote the establishment of broader partnerships and facilitate common development and prosperity on a larger scale [Ministry of Foreign Affairs of the PRC, 2017a].

Four days later, the 9th BRICS Summit was hosted under the theme "BRICS: Stronger Partnership for a Brighter Future" by China in Xiamen on 3 September 2017. During the summit, the BRICS Plus cooperation format was formally launched by China. Giving a keynote speech at the opening ceremony, Chinese President Xi Jinping [Ibid., 2017b] said "we should expand the coverage of BRICS cooperation and deliver its benefits to more people. We should promote the "BRICS Plus" cooperation format and build an open and diversified network of development partnerships to get more emerging market and developing countries involved in our concerted endeavours for cooperation and mutual benefits." The leaders of Egypt, Guinea, Mexico, Tajikistan, and Thailand were invited to the Dialogue of Emerging Market and Developing Countries under the theme "Strengthening Mutually-Beneficial Cooperation for Common Development" [BRICS, 2017]. The "BRICS Plus" was also featured in the Xiamen Declaration: "We shall also strive towards broad partnerships with EMDCs, and in this context, we will pursue equal-footed and flexible practices and initiatives for dialogue and cooperation with non-BRICS countries, including through BRICS Plus cooperation" [Ibid.].

The promotion of the BRICS Plus format can be interpreted in the context of the change of China's BRICS policy orientation. China wants to combine the BRICS and the BRI and put itself in a leadership role. Both BRICS and BRICS Plus are by the Chinese side seen as a mechanism to negotiate [Hooijmaaijers, 2019]. The Belt and Road Portal, for instance, mentions the BRICS' synergy with the BRI, as it states that "Although China's economy has surpassed the other four members of the BRICS bloc combined, China is willing to share its development premiums with them and the other developing countries. An important way is to form an extensive partnership network. BRICS and the BRI are both striving in the same direction" [Li, 2017].

Despite China's effort to promote the BRICS Plus format, it has received divergent responses from other BRICS members. The other four member countries remain wary of China's predominance in BRICS and its increasing influence in the Global South, especially India [Dasgupta, 2017; Purushothaman, 2019; Siddiqui, 2017]. Fearing China utilizes the group as a power multiplier, considering China's wider global strategy particularly through its BRI, India's concern is that the Plus format would boost China's influence while potentially eroding that of the other members. In the run-up to the 9th BRICS Summit held in China, the Indian delegates attending the academic forum in Fuzhou were steadfastly opposed to docking the BRI with the BRICS in the future [Naidu, 2018]. China had initially proposed the list of prospective members, which includes a diverse crowd from the Global South: Bangladesh, Egypt, Indonesia, Iran, Mexico, Nigeria, the Philippines, South Korea, Turkey and Vietnam

[Mpungose, 2017]. However, due to limited consensus within the grouping, only five countries mentioned above were invited to the Summit. The coherence of the outreach strategy has been challenged by its members' divergent interests and concerns.

### Parallel Regional Outreach With Africa and Diverse "Plus"

Building on the innovation of China, South Africa opted for a synthesis of the regional outreach format and the Plus format. From 25 to 27 July 2018, under the theme of "BRICS in Africa: Collaboration for Inclusive Growth and Shared Prosperity in the 4th Industrial Revolution," the 10th BRICS Summit was held by South Africa in Johannesburg [BRICS, 2018].

The BRICS Africa outreach session and BRICS plus session were held on the last day of the Summit on 27 July 2018. At noon, BRICS leaders invited the leaders of Ethiopia, Angola, Zambia, Namibia, Senegal, Gabon, Togo, Uganda, Rwanda (AU chair), and SADC leaders to the BRICS Africa outreach dialogue. Later, in the afternoon, BRICS leaders had Argentina (as Chair of the G20 and influential MERCOSUR member), Indonesia (as Co-Chair of the New Africa – Asia Strategic Partnership with South Africa and influential ASEAN member), Egypt (as Chair of the G77+China), Jamaica (as incoming Chair of Caribbean Community, CARICOM) and Turkey (as Chair of the Organization of Islamic Cooperation, OIC) at the BRICS Plus Initiative session. In total, 21 countries including emerging markets and African countries took part in the BRICS Plus leaders' dialogue.

After the Summit, China's South Africa ambassador Lin Songtian [Embassy of the People's Republic of China in the Republic of South Africa, 2018] made a long remark and highlighted the tangible and intangible benefits of the BRICS and the BRICS Plus mechanism for the host and partners. He praised how the Summit had further improved the BRICS Plus mechanism and expanded the developing partnership network of the BRICS "circle of friends." The outreach and BRICS Plus formats operated as tools for the soft involvement of geographically distant countries, located in different regions of the world, in joint activities on issues of mutual interest. Besides, following the BRICS-SCO-EAEU joint Summit in 2015, under the auspices of Russia, an agreement was concluded in 17 May 2018 between China and EAEU members to strengthen trade and economic cooperation, and many of the projects envisioned are part of the BRI [EEC, 2018].

### Stalled Outreach?

From 2013 till 2018, it seems that BRICS outreach practices – the regional outreach format and BRICS Plus format – had found some continuity. Over the past years, albeit dynamically, such practices had helped the members of BRICS and especially the hosts to further engage with their respective regions and diverse partners on common interests. However, neither a regional outreach nor the plus session took place during the 11th BRICS Summit on 13 and 14 November 2019 in Brasília. The Bolsonaro government insisted on inviting Venezuela's Juan Guaidó to the Outreach Summit. However, all other BRICS members do not recognize Guaidó as president. Brazil decided to cancel the Outreach Summit altogether before the Summit. Since 2013, this was the first time that the Outreach Summit did not happen and the move was privately criticized by diplomats from the other BRICS countries [Stuenkel, 2019].

This stalled outreach reflected a lack of cohesion on BRICS members' outreach strategies and priorities. Before the summit, at many meetings and occasions, China made it clear that it wanted the BRICS Plus to happen in 2019 [Ministry of Foreign Affairs of the PRC, 2019a; 2019b; 2019c]. Although the outreach was canceled, during the Summit, at the BRICS Business Forum on 13 November and in a formal statement on 14 November, Xi continually called on

the BRICS countries to leverage “BRICS Plus” cooperation as a platform to increase dialogue with other countries and civilizations and for BRICS to win more friends and partners [Ministry of Foreign Affairs of the PRC, 2019d; 2019e].

### *The BRICS Outreach/Plus via BRICS Institution: New Development Bank*

Over the past decade, we have witnessed the intensification of BRICS institutionalization. Beyond outreach via summits, the establishment of BRICS’ own institutions have made one more channel for its outreach.

Since 2012, BRICS has started working on establishing its own institutions. In 2014, significant progress of the BRICS institutionalization has been made – the Treaty for the Establishment of Contingent Reserve Arrangement and the Agreement on the New Development Bank were signed by BRICS leaders at the Fortaleza Summit. The former is a framework for the provision of support through liquidity and precautionary instruments in response to actual or potential short-term balance of payments pressures [BRICS, 2014a]. However, since the membership of CRA doesn’t open to non-BRICS countries, we leave it out of our analytical focus. The latter is formed to support infrastructure and sustainable development efforts in BRICS and other underserved, emerging economies for faster development through innovation and cutting-edge technology [NDB, 2019a]. The Bank’s initial subscribed capital is US\$50 billion and became fully operational in 2016 [Ibid., 2016]. A closer look at the development of NDB reveals following outreach features.

#### Open Membership

In terms of the membership, the NDB Agreement states it shall be open to members of the United Nations and shall be open to borrowing and non-borrowing members [BRICS, 2014b]. As being formulated, the Agreement gives the NDB a built-in outreach feature. This has laid the groundwork for the NDB to have substantial outreach, expansion, and cooperation with non-BRICS countries in the foreseeable future. In the 2019 Summit, notwithstanding neither of the regional outreach nor the plus session happened, for the first time, the leaders of BRICS put membership expansion of the NDB on agenda. As stated in the Brasília Declaration [Ibid., 2019], the expansion of the NDB membership in accordance with its Articles of Agreement will strengthen the Bank’s role as a global development finance institution and further contribute to the mobilization of resources for infrastructure and sustainable development projects in BRICS and other EMDC’s.

#### Regional Centres/Offices

Being aware that member countries have different systems and processes for project origination, the NDB has invested in learning to work with these systems and adopted country-specific approaches since its inception [NDB, 2019b]. As set in the Articles of Agreement, the NDB may establish offices necessary for the performance of its functions [BRICS, 2014b]. And as further clarified in the NDB’s General Strategy, identification and preparation of bankable projects in BRICS and other member countries are the main functions of the Bank’s regional offices [NDB, 2017a].

We have seen that after the Bank’s headquarters was built in Shanghai in 2016, three regional offices were established year by year. The first regional office of the NDB – Africa Regional Center (ARC) – was officially opened in Johannesburg on 17 August 2017. This is an important milestone for the Bank to set the ARC as an outreach office for sustainable infrastructure development in South Africa and as a visible participant in the development agenda

of the continent [NDB, 2017b]. On 26 July 2018, the second agreement – for the hosting of NDB's Americas Regional Office (ARO) in São Paulo – was signed [Ibid., 2018]. On 13 November 2019, the NDB and the Government of Russia Federation signed the Agreement on the hosting of the New Development Bank Eurasian Regional Centre (ERC) in the Russian Federation [Ibid., 2019c]. According to the Agreement, the ERC will be located in Moscow. Based on the NDB's business needs, the Bank may also establish premises in other cities within Russia [Ibid., 2019d].

These regional centers/offices play several roles for the NDB and its outreach. For instance, the ARC's role was defined by NDB President Kamath [Ibid., 2017c]: a) its initial role consisted of identification and preparation of projects in South Africa. This is in line with South Africa's National Development Plan, which the Government has adopted as a blueprint for the future economic and socio-economic development strategy for the country. The NDB and the ARC aim to partner with the Government in the achievement of these goals. In particular, the ARC plays an important role in preparing these projects so that they can be financed and supports the effective and efficient implementation of these projects. Furthermore, as the activities of the ARC will expand both in scale and in scope over time, b) it could play a role in sharing knowledge and development experience across countries. c) It could also play a role in coordinating NDB's partnerships and collaborations with institutions on the continent. d) And importantly, when the Board of Governors approves expansion of the NDB's operations in other countries in Africa, the ARC could also play a leading role in initiating and scaling up the NDB's work in those countries.

Up to now, the NDB has set up a presence in four continents headquarters in Shanghai, regional office/center in Sao Paulo, Johannesburg, and Moscow. Similar to ARC, the ARO and ERC will play important roles in each respective region. These regional centers/offices are also further evidence of the NDB's significant institutional development and should help the Bank secure a foothold in each continent [Ibid., 2018]. By working with strategic partners with strong implementation capability and a shared interest in infrastructure and sustainable development, they could make contributions to enhancing the Bank's overall impact [Ibid., 2017a].

### Global and Diverse Partnerships

In line with the NDB's mandate, the Bank is actively reaching out and engaging in partnerships with diverse actors to pool efforts in supporting global growth and sustainable development. The diverse partners consist of Multilateral Development Banks (MDBs, including major global and regional multilaterals as well as smaller sub-regional institutions), national development banks, commercial banks, enterprises, and academia. Take building partnership with MDBs as an example, the NDB has signed Memoranda of Understanding and Cooperation Agreements with eleven MDBs since 2016. Through the institutionalized partnership, the NDB seeks to undertake joint projects and knowledge exchanges with the World Bank and major regional MDBs (e.g. Asian Development Bank, European Investment Bank, European Bank for Reconstruction and Development) to make the most of their decades of experience. NDB is also engaging with development institutions controlled by EMDCs, such as the Asian Infrastructure Investment Bank (AIIB), the Development Bank of Latin America (CAF), the Eurasian Development Bank and the International Investment Bank.

Put together, these diverse partnerships have important functions for the NDB's performance: to enable the Bank to tap into the expertise of established development institutions; to better access local knowledge on borrowing countries' strategic development priorities, infrastructure and sustainable development issues, national laws and policies; to strengthen its ca-

capacity to assess and implement projects as well as increasing capillarity of its operations [NDB, 2017a].

## Explaining the BRICS Outreach

### ***BRICS Outreach Motivations***

In our theoretical framework, we considered the G7/8's and to some degree the G20's ambition for "group hegemony" [Bailin, 2005], feeding into three hypotheses for outreach related to effectiveness, legitimacy and socialization. The ambitions of the BRICS have thus far been more modest: similar to the G7/G8, the BRICS wants to contribute to global public goods that correspond with their own interests, but has never shown an aspiration to sit in the cockpit of global governance. However, the BRICS displays characteristics of a counter-group hegemony to the G7. Like the G7, the BRICS countries are held together by a degree of like-mindedness. They are state-permeated market economies [Nölke et al., 2015] that are keen on upholding international pluralism in terms of political and economic systems. They share a few grievances and aspirations with regard to the world order and multilateral system, and engage in soft balancing with the Western powers [Mielniczuc, 2013]. In other words, given their different state-society complexes [De Graaff, Van Apeldoorn, 2017], this counter-hegemony pursues a different "social purpose" [Ruggie, 1982] than the G7. Similar to the preponderance of a declining US in the G7, the BRICS both benefits and suffers from the preponderance of a rising China.

As to Hypothesis 1 (effectiveness), one of the most drastic ways of raising effectiveness through outreach was the adoption of South Africa as a full member after a short relationship. For the rest, the BRICS summits are not accompanied by much operational collaboration with outreach partners.

Hypothesis 2 (legitimacy) is to a larger extent confirmed. Rotating BRICS hosts are keen to invite regional neighbors, also establishing ties between the BRICS and regional forums. A similar motivation is visible in the Chinese-led BRICS Plus initiative. These outreach initiatives, and non-members participation to them, legitimize the BRICS and strengthen the image of these five as an alternative major power grouping to the G7.

Hypothesis 3 (socialization) is rather poorly confirmed since there is little operational cooperation that can function as a channel for socialization.

Hypothesis 4 (instrumentalization) is to a notable extent confirmed. The lack of group cohesion opens the door to more individual initiatives using the BRICS platform. In fact, as is also the case in the G7/G8 and G20, the consecutive hosts' regional-based outreach practices, clearly show the way the rotating chairs use the BRICS to enhance their bilateral ties with selected neighbors. In addition, the BRICS Plus efforts reveal China's individual strategy in function of its BRI, in which the BRICS is instrumentalized as a power multiplier – even leading to suspicion of the other members [Hooijmaaijers, 2019]. A similar problem came up in 2019 when president Bolsonaro of Brazil wanted to invite the controversial self-declared president Guaidó of Venezuela, which would have given the latter an extra boost of international prestige. This constituted a clear Brazilian foreign policy objective, to which the other BRICS members openly opposed.

In parallel, the NDB forms an exception to this relatively modest picture. We see indications of strong outreach motivation. Adoption of new members is enshrined in the founding document, the strategy and reconfirmed at the 2019 BRICS summit. This might add, depending on the newcomers, to capacity in terms of new capital and better credit ratings. The many partnerships between the NDB and national development banks, commercial banks and mul-

tilateral development banks must be understood in this context as well. The NDB's establishment of regional centers/offices and the adoption of country-specific approaches enables the Bank to improve its effectiveness [NDB, 2019b] (Hypothesis 1). This motivation will be shown more evidently when the expansion of NDB's membership occurs in the near future. In addition, projects in non-member developing countries will contribute to the global public good of infrastructure and green energy so as to advance the interests of BRICS countries in direct and indirect ways (Hypothesis 1). As to BRICS legitimacy (Hypothesis 2) and socialization (Hypothesis 3), the NDB offers opportunities.

Developing countries will regard the NDB as a form of more sensitive south-south cooperation and appreciate the weaker conditionality compared to the western-dominated multilateral development banks, which indirectly will consolidate the image of BRICS as a useful and necessary counter-hegemonic bloc. At the same time, NDB operations will function as a channel for socialization into BRICS approaches to development. However, since the NDB has chosen for substantial partnerships with other parties, including the western-dominated multilateral development banks, part of the BRICS socialization function will be diluted [Heldt, Schmidtke, 2019].

### ***BRICS Outreach Institutionalization***

Given the common interests and degree of like-mindedness within BRICS, the group could theoretically be well motivated to intensify and institutionalize its outreach. In reality, however, the group struggles to sustain its outreach activities. Unlike the G8's Africa and G5 outreach – which were rooted in a more coherent outreach strategy based on a more cohesive vision of the G8's role and ambition in the world – we do not see the BRICS working with a relatively fixed set of countries for some years.

One of the reasons is that BRICS summitry is still relatively young and that the institutionalization of a lesser priority than the consolidation of the group itself takes time. Still, during the outreach process some political problems came to the surface, which reflect deeper divisions within the group. Our research confirms Hypothesis 5 that the institutionalization of the BRICS outreach is a function of the cohesion of the BRICS outreach strategy, which in its turn is linked to the overall political cohesion of BRICS. Notably, distrust and divergence within the group explain why the BRICS Plus cannot take off as China would like.

What is quite well institutionalized, as we also see in the G7/G8 and G20, is the hosts' choice to invite a selection of regional neighbors. However, the actual selection of countries, as e.g. Bolsonaro's invitation to the self-declared president of Venezuela showed, can still be subject to opposition and rejection within the BRICS group.

The NDB, in contrast, is in itself an expression of strong BRICS institutionalization and a high degree of political cohesion within the thematic domain of infrastructure financing. Within its focused mandate and financial needs in terms of capital and credit ratings, it has a clear incentive for outreach beyond BRICS. This case learns that when a major power grouping creates its standalone multilateral organization, the latter can follow a coherent dynamic of its own, despite political divisions at the higher political levels of BRICS, even though important decisions – e.g. adopting new members of the Bank – will have to be rubberstamped by the BRICS top leadership.

What about the interests and agency of outreach partners? We do not see signs of opposition or reluctance. As mentioned, the BRICS does not risk to engage in a patronizing way with other major powers. One major power, South Africa, was soon adopted as a full member, avoiding that risk from the outset. The outreach partners are willing to be invited to this alternative prestigious club, the more so in a post-Cold War world in which developing and emerging countries like to

maintain good political and economic relations with both Western and non-western major powers alike. A case in point is Turkey, which at present has a number of serious issues with its Western allies, and is therefore all the more heartened by a BRICS invitation. The lack of institutionalization is not due to outreach partners' attitudes, unlike what happened to the G8+5 process.

## Conclusion

Major power groupings are evolving. As a relatively small major power grouping, BRICS has deepened its institutionalization and made its first steps to influence the global political economy in the past decade. However, research on the BRICS outreach remains a gap. Therefore, in this article, we probe into the why and how of BRICS outreach and focus on two interrelated puzzles: a) the motivations and b) the form and degree of institutionalization of the BRICS outreach. We define outreach here as collaborative interaction among the BRICS actors (governments and institutions) and other actors within and outside the BRICS area and we focus on outreach to governments of non-BRICS countries and national top officials representing regional organizations.

We offer a theoretical framework based on the experiences of Gx, considering both commonalities and differences with BRICS. In terms of the motivations of outreach, we draw from "group hegemony" theory to consider the BRICS as being in the initial stage of collectively shaping the global political economy as a counter-group hegemony to the G7. This feeds into three hypotheses for outreach related to effectiveness, legitimacy, and socialization. A fourth hypothesis pertains to the instrumentalization of BRICS outreach by individual members. In terms of the form and degree of outreach institutionalization, inspired by the Gx practices, we draw hypotheses for outreach related to political cohesion and power asymmetry.

At the level of the summit channel, HYP1 (effectiveness) was substantiated modestly. The inclusion of South Africa as a full member was the most drastic way of raising effectiveness. For the rest, the BRICS summits are not accompanied by much operational collaboration with outreach partners so far. HYP2 (legitimacy) is to a larger extent confirmed. BRICS outreach activities, and non-members participation to them, legitimize the BRICS and strengthen the image of these five as an alternative major power grouping to the G7. HYP3 (socialization), however, is poorly confirmed. HYP4 (instrumentalization) is to a notable extent confirmed. The lack of group cohesion opens the door to more individual instrumentalization of the BRICS platform as a power multiplier. For instance, the BRICS Plus reveals China's individual strategy in the function of its BRI, and the attempt of president Bolsonaro of Brazil to invite the controversial self-declared president Guaidó of Venezuela reveals Brazilian foreign policy interest. As to the NDB channel, HYP1 (effectiveness) is to a large extent confirmed, given the fact that open membership is enshrined in the founding document, the establishment of regional centers/offices, the adoption of country-specific approaches, the contribution to the global public good of infrastructure and green energy in direct and indirect ways. As to HYP2 (legitimacy) and HYP3 (socialization), the NDB offers opportunities.

In terms of the form and degree of outreach institutionalization, the development of BRICS outreach is an integral part of the overall BRICS institutionalization. It reflects the dynamics of its internal cohesion, how it positions itself in the world and how it is perceived by others. The group could theoretically be well motivated to intensify and institutionalize its outreach, however, at summitry, we find that the group struggles to sustain its outreach activities. Our research confirms HP5 that the institutionalization of the BRICS outreach is a function of the cohesion of the BRICS outreach strategy, which in its turn is linked to the overall political cohesion of BRICS. During the outreach process some political problems came to the surface, which reflect deeper divisions within the group. On the one hand, distrust and divergence with-

in the group explain why the BRICS Plus cannot take off as China would like. On the other, the BRICS *per se* is still relatively young; it takes time to further consolidate and institutionalize.

The NDB, in contrast, presents a stronger degree of outreach institutionalization. Actually, the NDB itself is an expression of strong BRICS institutionalization and a high degree of political cohesion within the thematic domain of infrastructure financing. Within its focused mandate and financial needs in terms of capital and credit ratings, it has a clear incentive for outreach beyond BRICS. When the expansion of NDB's membership occurs in the future and more outreach initiatives become operationalized, its influence will be increased and add to the overall BRICS impact.

In sum, this research intends to offer a contribution to the ongoing debate on BRICS and the under-researched BRICS outreach process as part of the overall BRICS institutionalization. Albeit fluctuant, the impact of BRICS outreach in direct and indirect ways should not be overlooked; it can be a long-term strategic investment by BRICS leaders. It creates extra channels for BRICS to consult, coordinate, and position themselves by fostering South-South consensus on several issues. And more importantly, it may help the BRICS to reach a more mature stage as a counter-group hegemony. To better assess the effectiveness and the implications of the still-new BRICS outreach, longer-term research is needed. Furthermore, BRICS is also outreaching with some non-state actors, such as BRICS Business Forum, BRICS Civil Forum, BRICS Youth Forum. In order to present a comprehensive picture of BRICS outreach, future research may include BRICS outreach with non-state actors.

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## Appendix 1: List of the BRICS Outreach/Plus Partners

List of the BRICS Outreach/Plus Partners							
No.	Year	Channel	Format	Country	Organization	Region	Outcome
1	2009	Summit	Outreach	South Africa		Africa	
2	2013	Summit	Outreach	15 African leaders		Africa	
3	2013	Summit	Outreach		Africa Union (AU)	Africa	
4	2014	Summit	Outreach		The Union of South American Nations (UN – ASUR)	South America	
5	2014	Summit	Outreach		The Community of Latin American and Caribbean States (CELAC)	Latin American & Caribbean	

List of the BRICS Outreach/Plus Partners							
No.	Year	Channel	Format	Country	Organization	Region	Outcome
6	2015	Summit	Outreach		The Shanghai Cooperation Organization (SCO)	Eurasia	
7	2015	Summit	Outreach		The Eurasian Economic Union (EAEU)	Eurasia / Central and northern Asia and Eastern Europe	8 May 2015 – Joint Statement on Cooperation on the Construction of Joint Eurasian Economic Union and the Silk Road Projects; 17 May 2018 – Agreement on trade and economic cooperation between the Eurasian Economic Union (EAEU) and the People's Republic of China (PRC); 10 Oct 2019 – Agreement on trade and economic cooperation between the Eurasian Economic Union (EAEU) and the People's Republic of China (PRC) entered into force
8	2016	Summit	Outreach		Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation countries (BIMSTEC)	South Asia & South-east Asia	BIMSTEC Leaders' Retreat 2016 Outcome Document
9	2017	Summit	Plus	Egypt		Africa	
10	2017	Summit	Plus	Guinea		Africa	
11	2017	Summit	Plus	Mexico		North America	
12	2017	Summit	Plus	Tajikistan		Central Asia	
13	2017	Summit	Plus	Thailand		Southeast Asia	
14	2017	NDB	Outreach	Africa Regional Center in Johannesburg (South Africa)		Africa	
15	2018	Summit	Outreach	Ethiopia		Africa	
16	2018	Summit	Outreach	Angola		Africa	
17	2018	Summit	Outreach	Zambia		Africa	
18	2018	Summit	Outreach	Namibia		Africa	
19	2018	Summit	Outreach	Senegal		Africa	
20	2018	Summit	Outreach	Gabon		Africa	
21	2018	Summit	Outreach	Togo		Africa	

List of the BRICS Outreach/Plus Partners							
No.	Year	Channel	Format	Country	Organization	Region	Outcome
22	2018	Summit	Outreach	Uganda		Africa	
23	2018	Summit	Outreach	Rwanda		Africa	
24	2018	Summit	Outreach		African Union (AU)	Africa	
25	2018	Summit	Outreach		The Southern African Development Community (SADC)	Africa	
26	2018	Summit	Plus	Argentina	As Chair of the G20 and influential MERCOSUR member	South America	
27	2018	Summit	Plus	Indonesia	As Co-Chair of the New Africa – Asia Strategic Partnership with South Africa and influential ASEAN member	Southeast Asia	
28	2018	Summit	Plus	Egypt	As Chair of the G77+China	Africa	
29	2018	Summit	Plus	Jamaica	As incoming Chair of CARICOM	Caribbean Sea	
30	2018	Summit	Plus	Turkey	As Chair of the OIC	Western Asia & Southeast Europe	
31	2018	NDB	Outreach	Americas Regional Office in Sao Paulo (Brazil)		Americas	
32	2019	NDB	Outreach	Eurasian Regional Centre Moscow (Russia)		Eurasia	

# The Role of BRICS in International Development Assistance

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## Abstract

*With their growing economic power and international influence, the BRICS group of Brazil, Russia, India, China and South Africa are paying increasing attention to international development assistance. Although the BRICS countries started later than western developed countries, the speed of their development is staggering and their share in foreign aid is gradually increasing. The BRICS countries continue to innovate forms of assistance and cooperation in their own international development assistance, to strengthen cooperation with recipient countries, and to plan their own foreign aid work through the establishment of relevant institutions and the publication of relevant documents. But, at the same time, the BRICS countries are facing certain challenges in the process of international development assistance. This article examines the historical practice of BRICS' international development assistance, analyzes the role BRICS plays in international development assistance, and considers the future prospects for BRICS' participation.*

**Key words:** BRICS; international development assistance; China's efforts

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## International Legitimacy and BRICS International Development Assistance

In this article, we assume that strive of BRICS to improve its own and overall international legitimacy is one of the keys to explain the growing role of BRICS countries in international development assistance system. We define legitimacy as a belief within a given constituency or other relevant audience that a political institution's exercise of authority is appropriate [Tallberg, Zürn, 2019]. In other words, only legitimate institution can set norms and rules that will be followed by actors. Except for the rulemaking, other main functions of legitimacy include trust-building and agenda-setting. The latter two also serve for the first one, just in order to empower its capacity to develop new norms.

There are three main dimensions of international legitimacy, which are: procedural, performance and substantive. Procedural legitimacy outlines the importance of right process within the institution, while performance legitimacy focuses on the right way of actions performed by institution. And substantive legitimacy is the significance of the values and substantive agenda of an institution. Between all aforementioned dimensions, we suggest that performance legitimacy applies most effectively for BRICS, as its countries impressive economic performance and, therefore, rapidly increasing “global development assistant” potential, may be seen as the major legitimizing factor for BRICS. This factor is also possible to stimulate the shaping of two other dimensions.

By now, procedural and substantial legitimacy are not that significant, when it comes to BRICS. First of all, BRICS is undoubtedly an international institution, but not in the traditional sense, which suppose that international institution should have a certain structure, with the joint ruling body or mechanism, that implement policy and have a set of procedures. BRICS is more an intergovernmental platform, which coordinate policies between member countries and has a lack of procedural order. Secondly, as it consists of the very different countries, it is harder to set a common agenda on various issues or construct common values, so in the decision-making process, consensus is needed.

## Summary of the BRICS International Development Assistance Policy

The growth of the BRICS countries is extremely rapid. The economic development of the BRICS countries is even faster. In 2018, the average GDP growth of the BRICS countries was 5.7%, contributing 43.2% to the world economic growth. According to purchasing power parity (PPP), the BRICS global GDP share rose from 27.2% in 2010 to 32.7% in 2018, greater than the total of G7 added up [NDB, 2019]. After the establishment of the BRICS cooperation mechanism, the scale of economic development of various countries has advanced by leaps and bounds. The role of emerging economies in international development assistance has become increasingly prominent because of the growing national strength of the BRICS countries. According to the Development Assistance Committee, between 2011 and 2014, non-OCED countries increased their foreign aid by \$17.6 billion from the \$14.1 billion, accounting for 18.7% of the 2014 foreign aid quota [Zhao, Jing, Ouyang, 2018].

Although the BRICS countries are based on economic and trade cooperation, since the first summit of the BRICS countries, international development assistance has become a priority for the BRICS countries. This matter ranked fifth (6.3%) in the words and documents of the BRICS countries, and fourth in the number of all BRICS obligations [RANEPACIIR, n. d.]. The table below demonstrates how the BRICS international development agenda and policy have been shaping throughout the years.

This timeline reveals three focal points, which underpin international development policy of BRICS countries. First, it strongly complies with global frameworks, related to international development assistance. For instance, adherence to implementation of UN Sustainable Development Programs, whether Millennium Development Goals (2000–15) or the new Sustainable Development Agreement (2015–30), starting from the very first summit, is the important part of BRICS international assistance agenda and even loom larger within the years.

Second, the “toolkit” of the BRICS international development policy has broadened from simple humanitarian assistance and foreign direct investment (FDI) to more advanced instruments, such as: trade, development financing and etc. In this sense, a decision to establish BRICS New Development Bank (NDB) in 2013 was a crucial achievement.

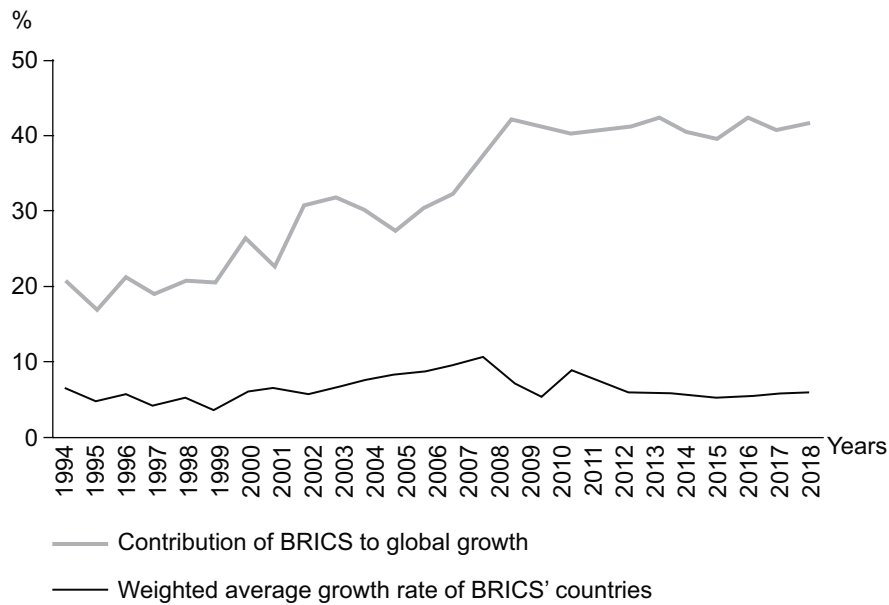


Fig. 2. BRICS Countries and Their Contribution to Global Economic Growth

Source: [NDB, 2019].

Table 1. Contents Related to International Development Assistance in Each BRICS Summit

No	Date	Location	Content Related to International Development Assistance
1	16 June 2009	Yekaterinburg, Russia	1. Emphasize the important role of international trade and foreign direct investment in economic recovery. 2. Implement the concept of sustainable development. 3. Cooperate in key social areas
2	15 April 2010	Brasilia, Brazil	1. Promote multilateral, comprehensive and sustainable development of the world economy. 2. Expand cooperation on global issues to promote world economic recovery and sustainable growth. 3. Ensure that developing countries achieve the UN Millennium Development Goals by 2015
3	14 April 2011	Sanya, China	1. Conduct global economic governance on the basis of mutual respect and collective decision-making. 2. Strengthen cooperation in the fields of economy, finance and trade to ensure the strong development momentum of the BRICS countries. 3. Call for the implementation of the reform goals of the International Monetary Fund proposed by the G20, and increase the voice of emerging economies and developing countries. 4. Regulate the commodity trading market
4	29 March 2012	New Delhi, India	1. Work with all parties to address opportunities and challenges with developed and developing countries. 2. Explore the possibility of building New Development Bank and provide development finance for BRICS and other developing countries. 3. Promoting growth and sustainable development is the goal of the BRICS countries and is essential for economic development, poverty eradication and hunger in many developing countries

No	Date	Location	Content Related to International Development Assistance
5	27 March 2013	Durban, South Africa	<ol style="list-style-type: none"> <li>1. Encourage foreign direct investment, knowledge exchange, capacity building, and African trade integration to support African industrialization.</li> <li>2. The BRICS countries can raise funds and agree to establish a New Development Bank. Ensure that developing countries have access to long-term, stable financing channels from a variety of sources.</li> <li>3. The United Nations should be the center and fulfill its commitments in the outcome of the international conference</li> </ol>
6	15 July 2014	Fortaleza, Brazil	<ol style="list-style-type: none"> <li>1. The BRICS countries seek peace, security, development and cooperation, deepen mutual relations, and realize a new vision of openness, tolerance, cooperation and mutual benefit.</li> <li>2. The BRICS economic growth and socially inclusive policies help stabilize the world economy, reduce poverty and eliminate inequality.</li> <li>3. Information technology can be used as an important tool for achieving sustainable social development, promoting the development of renewable energy and reducing energy consumption.</li> <li>4. Support the development of African social and economic development, especially the infrastructure and industrialization process</li> </ol>
7	9 July 2015	Ufa, Russia	<ol style="list-style-type: none"> <li>1. Develop relations between BRICS countries and emerging economies, other developing countries and other international and regional organizations.</li> <li>2. Emerging markets and developing countries are important drivers of future social and economic development. Structural reforms, domestic adjustments, and innovations should be emphasized</li> </ol>
8	16 October 2016	Goa, India	<ol style="list-style-type: none"> <li>1. The 2030 Agenda focuses on poverty eradication and calls on developed countries to fulfil their commitments of 0.7% of GNI for international development assistance, and to implement the 2030 Sustainable Development Agreement in line with national conditions</li> </ol>
9	3 September 2017	Xiamen, China	<ol style="list-style-type: none"> <li>1. Reaffirming its commitment to the implementation of the UN 2030 Sustainable Development Agreement, advocating inclusive development, balanced and coordinated development and cooperation models, supporting UN agreements.</li> <li>2. Develop a green and low-carbon economy based on efforts to eradicate poverty and sustainable development, strengthen cooperation in climate between BRICS and other emerging countries.</li> <li>3. Determined to build a more efficient economic governance structure, increase the voice and representation of emerging economies and developing countries, and create a more effective tax system</li> </ol>
10	25 July 2018	Johannesburg, South Africa	<ol style="list-style-type: none"> <li>1. Share economic results in a more powerful and inclusive manner and build an orderly external environment.</li> <li>2. Establish a transparent, non-discriminatory and open market order based on rules, and strengthen the construction of the multilateral trading system.</li> <li>3. The BRICS countries should invest heavily in infrastructure on the basis of reciprocity to support the development of industrialization in Africa</li> </ol>
11	13 November 2019	Brasilia, Brazil	<ol style="list-style-type: none"> <li>1. BRICS reiterate the importance of the implementation of the 2030 Agenda for Sustainable Development and call for redoubled efforts for its timely implementation.</li> <li>2. BRICS call on developed countries to fully implement their Official Development Assistance (ODA) commitments and to provide developing countries with additional development resources.</li> <li>3. BRICS urge developed countries to scale up the provision of financial, technological and capacity building assistance to developing countries to support mitigation and adaptation action to a climate change</li> </ol>

Source: Authors.

Third, areas of BRICS international development assistance also evolved. During the first few years of BRICS existence, its countries were mostly emphasizing the importance of international development assistance in fields like food safety, reduction of poverty, education

and energy. However, starting from 2015 and 2016 summits, BRICS countries international development policy have also focused on issues like social security, innovation, mitigation and adaptation to climate change.

## The Role of the BRICS Countries in International Development Assistance

The model of the BRICS countries broke through the old road of political and military alliances in the past, and came out with a unique new relationship of non-alignment which have broken through the restrictions and constraints of ideology and have embarked on a new path of mutual respect and common progress. In the traditional model, nation states are willing to share power with the international system, but unwilling to share legitimacy, thus bringing challenges to the international system. In the past, it was difficult to conduct win-win cooperation, and the sole winners were able to achieve true multifaceted cooperation and coordination, but the BRICS countries are different. The cooperation and foreign aid of the BRICS countries are based on mutual benefit and mutual benefit. The basic principles are unfolding. The BRICS countries coordinate their actions, strengthen coordination, and jointly promote international development assistance. We point out three main roles of BRICS in IDA system, which are innovator, booster and haven. This section will set out the role that should be played by BRICS countries (and particularly China) in international development.

### ***Innovator to the Patterns of Assistance***

When Chinese President Xi Jinping met with other G20 leaders in Osaka on June 28, noted that BRICS countries should promote the “innovative BRICS” network, adhere to multilateralism, and seek common development and revitalization with other emerging market countries and developing countries [Xinhua wang, 2019]. First of all, the BRICS countries should continue to pay more attention to equal and “green” development. A great way of BRICS to help developing countries in sustainable development is NDB funding. NDB applies sound banking principles to all businesses, ensures adequate compensation and considers risks, provides loans and other business support through guarantees of public or private financial instruments, and can also jointly provide guarantees with international financial institutions and other commercial banks without any politically attached conditions. According to the NDB 2017 annual report, five countries invested a total of \$1400 billion in 2017. Sustainability and infrastructure assistance are important concerns for NDB’s future development, and NDB will provide three fifths of financing for projects that integrate economic, environmental and social standards throughout the lifecycle over the next five years [NDB, 2018]. In the 2018 annual report, NDB is estimated to achieve 35 trillion US dollars in infrastructure investment in 2030, infrastructure investment will reach SDGs with an average growth rate of 26.3%, and BRICS infrastructure investment is expected to rise from 40.1% in 2018 to 42.5% in 2030, compared with 1.1% of G7 and 1.9% of growth in other countries [Ibid., 2019].

However, developed countries also attach great importance to sustainable development and institutions led by developed countries, such as the World Bank and the IMF, have long pursued aid policies with additional provisions. In the 1990s, the amount of IMF additional clauses reached its peak, with 73 adjustments to the structure of Thailand, 94 to South Korea, and more than 140 to Indonesia. The World Bank has similar operations. Zhu Jiejin observes that during the 1980s, the World Bank introduced a structural adjustment plan, and in 1999, its *Poverty Reduction Strategy Papers* (PRSPs) could be considered as a reference for additional

provisions [Fudan daxue jinzhuan guojia yanjiu zhongxin, 2016]. In the framework of OCED – DAC, aid is separated from trade and investment, so that donor countries and recipient countries are in an unequal position. As for China, it has changed its aid methods with political conditions in the past, and truly unconditionally helps difficult countries improve their livelihood. In 2015, Chinese government proposed that China should achieve carbon dioxide emissions by 60–65% compared with 2005, and non-fossil energy accounts for 20% of primary energy consumption. The data was 15% in 2009. The amount of forest savings in the 2015 target is about 4.5 billion cubic meters [Ibid.]. The emerging countries represented by China regard green development and sustainable development as important targets for foreign aid, and achieve green prosperity for themselves and recipient countries.

### ***Booster as a Gradually Rising Star***

The BRICS countries are important participants in international development cooperation, and the proportion of foreign aid at this stage is gradually increasing. Although some BRICS countries have a relatively late process of international development assistance, the momentum of the BRICS countries has maintained a strong momentum. The countries of the South gradually accumulated their own experiences in the development process and began to share the development experience. The foreign aid of the traditional OCED-DAC countries accounted for 0.29% of the gross national income in 2014, far below the target of 0.7% of its commitment, and also lower than the share of the early 1990s. Total official development assistance from 2010 began to decline. In 2014, the share bilateral aid for OCED-DAC countries and underdeveloped countries was 16% lower than in 2013 [Huang, 2018]. At the same time, BRICS countries are pumping up their foreign aid budgets, thus boosting global amount of IDA expenditures. For instance, in 2014, *White Paper on China's Foreign Aid* issued by China State Council revealed that amount of China's foreign aid in 2010–12 was 89.34 billion yuan (\$12.67 billion) and now continuously growing throughout the years [Information Office of the State Council of PRC, 2014].

Basically, this boost is the result of the economic globalization and political multipolarization that has brought a precious period of economic development to the BRICS countries. The world's wealth has reversed, and capital flows to developing countries, which is conducive to the accumulation of capital in emerging countries, so that emerging countries represented by the BRICS countries have invested in foreign aid [Li, 2012]. Some countries (such as Russia) successfully transformed from recipient countries to the status of foreign aid countries. According to the Russian Satellite News Agency, in 2016, Russia provided international development assistance to other countries or international organizations amounting to one billion US dollars, this figure is almost 10 times than the number of foreign aid in 2005 which was \$101 million and it is almost equal to the expenditure of housing public utilities and the media industry [Elusi weixing tongxunshe, 2017]. In addition, Marina Larionova in *Russia: A Re-emerging Donor* article notes, that IDA budget of Russia in 2004 was \$100 million, this figure reached \$785 million in 2009, nearly eight times that of 2004 [Larionova, Rakhmangulov, Berenson, 2016].

To enhance the implementation and coordination of its IDA policy, China have established National Agency for International Development Cooperation in March 2018. The department reports directly to the State Council and is responsible for formulating China's foreign aid strategy, policies, and coordination of various issues. The projects under the responsibility of the National Agency for International Development Cooperation mainly include a complete set of projects, which includes four ways: provide assistance to the recipient countries with engineering equipment, through the organization of all or part of the production and processing; provide basic living materials and technical service to the recipient countries; provide technical

assistance, dispatch experts and skilled workers to help recipient countries to achieve certain goals; conduct human resources development projects, through providing provide recipient countries with various forms of academic degree education, personnel exchanges and senior experts, volunteers and other services. Other important function of this institution is to promote cooperation between related department in various countries. On that institutional level, National Agency for International Development Cooperation held consultations with its Japanese counterpart – Japanese International Development Policy Department in June 2019.

### ***Haven for All Needed Countries***

This concept comes from Melaku Muluaem, director of the training department of the Ethiopian Institute for Diplomatic Relations. The BRICS countries have become one of the most important international organizations in the world and are becoming a safe haven for other developing countries and poor countries with a more positive attitude [Melaku, Li, 2017]. The world today still faces very serious imbalances in development and poverty. Many developing countries still face the impact of globalization and bottlenecks in development. In his speech at the opening ceremony of the BRICS Business Forum on 3 September 2017, Xi Jinping pointed out that the world economy is recovering, emerging countries and developing countries are performing well, and a new round of scientific and technological revolution and industrial transformation are poised for reform and innovation. The trend is moving forward. But on the other hand, 700 million people are suffering from hunger, tens of millions of refugees have been displaced, and countless people and innocent children have been killed. The world economy is in a period of adjustment of sub-health status and weak growth. There are many uncertainties in economic globalization. Therefore, it is necessary to deepen the cooperation in the BRICS, establish itself on its own, promote structural reforms, assume social responsibilities, and safeguard world peace [Xinhua wang, 2017].

The BRICS countries are promoting the balanced development of emerging countries and underdeveloped countries through the “BRICS+” cooperation model and become a safe haven for poor countries. Aid experience of western countries have provided direction for BRICS. A large amount of aid funds from OCED countries have flowed to the field of social development, such as agriculture and forestry, and the lack of attention to the infrastructure sector has also provided lessons for the BRICS countries [Fudan guoji guanxi pinglun, 2016]. BRICS have learnt great experience, focusing on the comprehensive development especially in infrastructure, at the same time, strengthened cooperation in humanitarian assistance, making humanitarian assistance activities one of the most important parts of the BRICS agenda. In 2011–2013, the number of external humanitarian assistance from BRICS countries was 6%. (\$0.8 billion) increased to 11% (\$1.4 billion). The BRICS countries attach importance to the eradication of poverty and hunger, especially in the backward areas of Asia and Africa [Degterev, 2014]. In addition, the BRICS countries are implementing projects in the fields of health, education and technological development in Asia and Africa.

Whilst providing a great amount of aid for Africa, the BRICS countries are also adopting an inclusive attitude and achieving international development assistance to Africa on the basis of respecting the path of equality among African countries in their own way of development rather than coercion. According to statistics, in 2012, the total trade volume of BRICS countries to Africa reached 340 billion US dollars, accounting for 27% of total African trade. The share of Africa’s trade has risen nearly tenfold from a decade ago. In comparison, the European Union’s trade in Africa during this year was 34%. At this stage, although developed countries still occupy a very large proportion of trade with Africa, it can be seen from Figure 2 that the amount of official development assistance in developed countries is declining, while the contribution of

emerging countries represented by BRICS countries It is gradually rising. In 2011, among the top 20 African trading partners, the trade volume of developed economies to Africa was 390.2 billion euros, and that of emerging countries represented by BRICS countries was 277.3 billion euros [Fudan guoji guanxi pinglun, 2016].

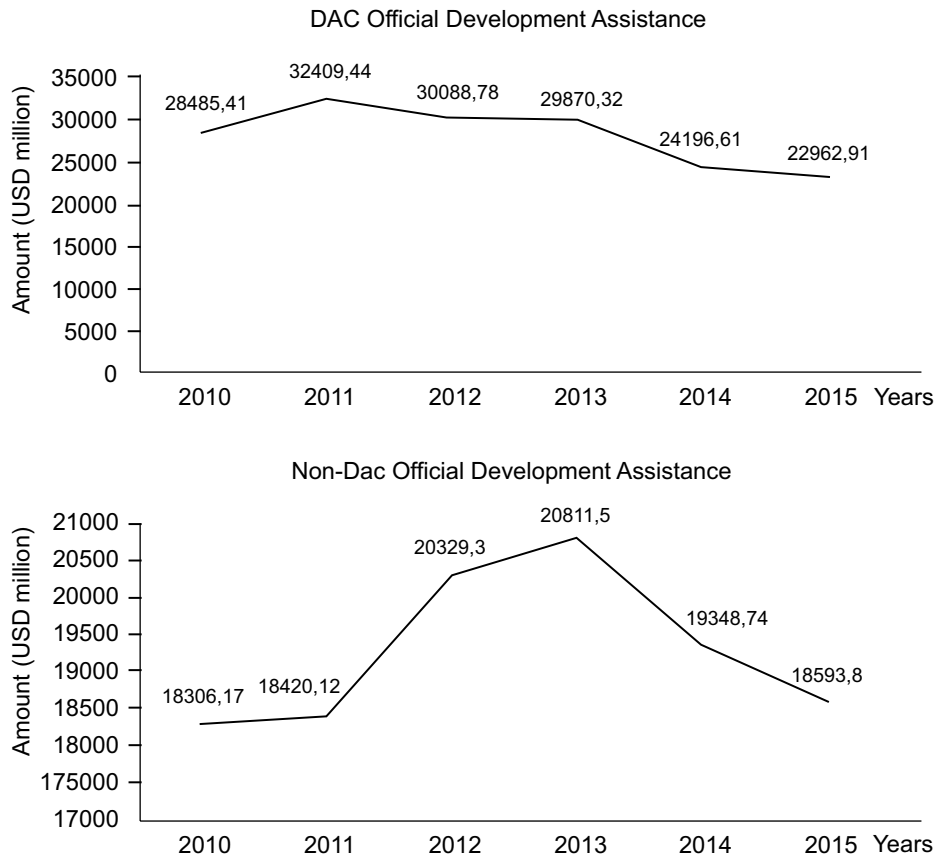


Fig. 2. Trends in DAC Countries' Aid to Non-DAC Countries Versus Africa

Source: [Africa Economic Outlook, n. d.; data from authors].

## The Future of BRICS Participation

### **Prospects for the Future of BRICS Foreign Aid Work**

**Leading the international Development Assistance.** The BRICS international development assistance started relatively late compared to developed countries, and BRICS countries such as Russia, China, and India were also recipients. However, the current state of foreign aid in the BRICS countries is gratifying, and has created a model of assistance, which is different from traditional Western powers and focusing on trade, peace and sustainable development. In 2010, when Western countries reached a peak in foreign aid, foreign aid fell by 3% in 2011. In 2011, OECD countries invested \$133.5 billion in foreign aid, and its amount still did not reach the UN target of 0.7%. 16 of 23 OECD countries have reduced their foreign aid budgets [Huang, 2013]. However, the emerging economies represented by the BRICS countries not only seize

the opportunity of the world economic development, but also vigorously develop their own economic strength.

Taking China as an example, China's Reform and Opening-up policy have succeeded. Most of the people have got rid of poverty and achieved a well-off society. China also actively participate in the process of international development assistance and become an important force for foreign aid. The BRICS countries actively respond to the UN's Millennium Development Plan and the 2030 Sustainability Agreement, bringing development opportunities and aid funding to poor areas. In the future, the BRICS will maintain an open, inclusive and mutually beneficial approach to assistance, improving the infrastructure and commodity markets of the recipient countries and recipient countries, providing foreign aid on the basis of developing their own economies. As an important part of diplomatic work, the proportion of international development assistance has shown an overall upward trend, and it has continued to move closer to the aid share of developed countries.

**Improving of the Assistance System by Cooperating With UN.** Due to the fierce competition between developed countries and emerging economies in international development assistance field, both sides hope to expand their influence through foreign aid and receive the support of the international community. Therefore, they have provided decent assistance conditions for recipient countries. Recipient countries have certain principle rights, so the choice between developed countries and BRICS will intensify competition between the two sides, which resulting in the fragmentation of the overall aid system, development of national foreign aid programs and the participation of the countries in international development assistance, and it is also likely to cause waste of aid resources. In the future process of foreign aid development, BRICS countries won't only cooperate between each other on internal affairs, but also increase the joint efforts of BRICS countries in foreign aid field. At the same time, they will work together with other emerging countries to contribute to poverty eradication, sustainable development.

Both developed and emerging countries are committed to providing foreign aid in accordance with the *UN 2030 Sustainable Development Agreement* and to abide by their commitment to the people of the world. As a representative of non-governmental organizations, the United Nations is playing an increasingly important role in international development assistance. The United Nations launched the *2030 Sustainability Agreement* in 2015, which stated that sustainable development should be based on inclusive attitudes, equality and mutual benefit, with a focus on poverty eradication efforts to address rising economic inequalities and social deprivation [Nan nan hezuo jinrong zhongxin, 2017]. BRICS emphasized support for the United Nations, including its high-level political forum on sustainable development, advocating fair/comprehensive/inclusive development, and an equitable and coordinated economic development model, and urged developed countries to complete development assistance commitments on time and provide more resources for developing countries.

**Promote Investment in the "Aid for Trade" System.** The inclusion of trade in the process of international development assistance is the innovative act made by BRICS. In the case of non-trade aid, the United Nations Trade Development Organization statistics show that in 2010, amount of foreign investment in Africa was \$308.74 billion, for developed countries the proportion was 77%, and 13.8% for BRICS countries. That period was an initial stage in international development assistance for emerging economies, represented by BRICS countries. Since 2012, the volume of merger and acquisition conducted by emerging economies have also far surpassed that volume of developed countries. After being affected by the financial crisis, western countries have shown negative values for non-mergers. Although the BRICS countries have also received certain fluctuations, they are still at the overall rising stage. In terms

of greenfield investment in Africa, the proportion of non-greenfield investment in developing countries increased from 42.5% to 63% in 2011, while that in developed countries decreased from 54.6% to 36.9% [Fudan guoji guanxi pinglun, 2016]. In the future, the BRICS countries should continue to expand their investment fields, continue to exert their strengths in construction, electronics, warehousing and communication, and at the same time innovate investment areas, attach importance to sustainable energy development and construction, and continue to promote Aid for Trade system.

### ***Difficulties and Challenges***

**Insufficient Infrastructure and Funding.** BRICS countries still do not match the speed of economic development and the scale of economic development. Infrastructure is an important tool to support a country's economic construction and people's happiness index, and is also an important basis for a country's foreign aid. The BRICS countries face the embarrassing situation of insufficient infrastructure construction and dragging down economic competitiveness. According to the Global Competitiveness Report 2014–15, China, Russia, South Africa, Brazil, and India rank 86th, 74th, 59th, 120th, and 90th, and these countries rank 28th 53th, 56th, 57th, 71th in competitiveness. BRICS countries generally face a situation of strong competitiveness and backward infrastructure. In order to cope with this situation, the BRICS countries have also begun to build infrastructure.

Russia introduced the Russian Railway Transport Development Strategy 2030 and plans to build a railway with a total length of 20,000 kilometers by 2030, of which 5,000 kilometers will be a high-speed railway, and the planned investment will reach 14 trillion rubles [Gao et al., 2015]. China vigorously promotes the construction of clean energy and invested 291 million dollars to build a clean energy project in Guangdong, and promote the development of domestic infrastructure, such as the Luoyang subway project. India will also invest about \$1 trillion in infrastructure to build infrastructure projects including electricity, roads, ports, and communications. The Brazilian government also issued a corresponding document in 2012, in which the Brazilian government plans to invest \$65.6 billion in the cost of building high-speed kilometers and railways over the next 20 years. In 2015, the Brazilian government enacted a second phase of transportation infrastructure investment plans, with an estimated investment of \$64 billion. South Africa will aim to break through the bottleneck in infrastructure construction, investing \$74 billion in infrastructure construction and will continue to expand the scale of infrastructure construction [Ibid.].

**Lack of Aid Documents and Regulations.** Unlike the general international organizations, the BRICS countries do not have a programmatic document as a guide in the economic and political development of the five countries because of their unique mode of cooperation and non-alignment and the development of inclusiveness. These assistance norms are necessary conditions to ensure agents formulate rules and ensure rules can be observed. Only normative constraints can ensure that people who obey the rules have a certain degree of consciousness to abide by the relevant rules or not interfere with others' obedience. This is a manifestation of the right of international governance to rule. Although China has promulgated the China Foreign Aid (2014) White Paper, and Russia has issued its foreign aid concept, but fundamentally, these documents are not a programmatic and can be coordinated.

The documents of the BRICS countries in achieving international development assistance cooperation do not have legal effect. One manifestation of the lack of programmatic documents is that the BRICS countries will encounter a strange circle in foreign aid, that is, the recipient countries need assistance needs, and the aiding countries will analyze, assess and determine

the final aid plan. This is “demand-driven” [Zhao, Ying, Ouyang, 2018]. In the absence of assistance applications, aid donors rarely voluntarily propose foreign aid, which is difficult for countries to incorporate foreign development assistance into their own development plans. China actively provides medical assistance to 69 countries in Asia, Africa, Latin America and the Caribbean and Oceania [Renmin wang, 2015].

## Conclusion

At a time when international development assistance is highly valued by the global community, BRICS became a major emerging force in this field. Since the establishment of this format, its role within IDA system have grown substantially, not only in terms of quantity, but also in terms of quality. First of these qualitative changes is the shift of the identity, most of the BRICS countries used to be recipients of foreign aid during certain periods of their history, but now actively dealing with the status of non-traditional donors. At the same time, BRICS nations (except for Russia) still position themselves as the developing countries and therefore act as a “haven” for other low-income states, attach great importance to the economic development of poverty-stricken areas and setting new standards for inclusive and equal assistance. Second, foreign aid strategy of BRICS has evolved from extensive usage of humanitarian assistance to more complex projects that involve flows of money, science and technology, education, knowledge sharing, trade and other measures. These new instruments, along with the new issues (like climate change), that shape modern IDA agenda, allow BRICS to take roles of “innovator” and “booster” of the international development assistance.

However, it should also be noted, that there are still certain problems with the current BRICS participation in international development cooperation, such as insufficient infrastructure construction, funding gap, and lack of assistance documents and regulations. But despite these challenges, BRICS also have some favorable conditions, both internal and external. At first, BRICS countries are improving their cooperation model, and join its forces to build a “BRICS+” platform. At second, support from the UN, World Bank and other major international institutions. In the future, the participation of BRICS in international development assistance has bright prospects. In the future, the participation of BRICS in international development assistance has bright prospects. Five countries have embarked on a new road of developing their own strength, grasping the opportunities of economic globalization and will take the lead in improving international development assistance system within the framework of UN 2030 Sustainable Development Agreement. In providing joint and its own IDA policy, China will rely on the National Agency for International Development Cooperation, which have to coordinate with other departments to work out national foreign aid programs. Finally, development assistance is the really important tool to shape an international legitimacy, which allows to resist multilateral competition pressure and unilateral action.

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# Filling Global Governance Gaps in Cybersecurity: International and European Legal Perspectives

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## Abstract

*The many recent cyber incidents have shown how cybersecurity has entered the realm of international relations. Several international organizations have taken cybersecurity policy initiatives, notably the United Nations (UN) and the European Union (EU). Both organizations aspire to a leading role in enhancing cybersecurity resilience. To date, however, these initiatives have not resulted in much regulation. This article examines which factors make lawmaking and the regulation of cybersecurity difficult at the international level, and whether some of these impediments are shared at the EU legislative level. Are difficulties in regulating cybersecurity embedded in the normative processes at the UN or the EU, or are they inherent to the high-tech phenomenon of cyber? As for the UN, the article looks at the work of the UN Group of Governmental Experts (GGE). While previous reports of the UN GGE seemed to point to an emerging international opinio juris, recent developments in the UN General Assembly (UNGA) show a strongly divided international community. At the EU level, the article discusses the two main legislative initiatives on cybersecurity that have seen the light of day: the 2016 Directive on Network and Information Security and the 2019 EU Cybersecurity Act.*

**Key words:** cybersecurity; global governance; international law; European Union; lawmaking; regulation; policy; UN GGE; Open-ended Working Group; NIS Directive; EU Cybersecurity Act

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## Introduction

Over the first two decades of this millennium, cybersecurity has become omnipresent within international relations. Yet, while clearly a policy concern, it has generated very little international regulation up to now. A straightforward reason that partially explains this inertia, is that the scope, nature, meaning, and terminology of cybersecurity are unclear [Futter, 2018, p. 202; Nye, 2016/17, p. 68].<sup>1</sup> There is little general agreement about what cybersecurity entails [European Court of Auditors, 2019], and it seems that different people use the term differently, de-

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<sup>1</sup> According to Futter [p. 209], the terminological vagueness is not without practical impact: the definition of cybersecurity in a given context is after all contingent upon what and who is being deterred, how, and whether the attribution of capabilities is possible. “The vague language means that it can be unclear who should

pending on the context [Futter, 2018, p. 205; Kosseff, 2018, p. 995; Kshetri, 2016, p. 3; Schatz, Bashroush, Wall, 2017, pp. 53–7]. This article focuses on cybersecurity *sensu stricto*, excluding a focus on the specific threats of cybercrime [Kshetri, 2016; 2009, pp. 141–4],<sup>2</sup> cyber terrorism [Harrison Dinniss, 2018, pp. 45–50; Ivanov, 2015, pp. 55–69; Fidler, 2015, pp. 10–1] and cyber warfare.<sup>3, 4</sup> This article does not study organizations that have taken policy or legislative initiatives on one of those specific threats.<sup>5</sup> In the United Nations (hereinafter: “UN”) context, cybersecurity has been defined by the International Telecommunication Union (hereinafter: “ITU”), a definition which has been further refined by Kshetri: “cybersecurity involves technologies, concepts, policies, processes and practices used to protect assets (e.g. computers, infrastructure, applications, services, telecommunications systems, and information) and the cyber environment from attack, damage and unauthorized access” [ITU, 2008].<sup>6</sup> In the European Union (hereinafter: “EU”) context, the following definition is used under the Cybersecurity Act: “cybersecurity means the activities necessary to protect network and information systems, the users of such systems, and other persons affected by cyber threats” [EU, 2018, Art. 2(1)].

Many policy initiatives regarding (different (sub)domains of) cybersecurity have been initiated, notably within the UN<sup>7</sup> and the EU contexts.<sup>8</sup> Both organizations aspire to a leading role in enhancing cybersecurity resilience. As both organizations have interesting – but very different – lawmaking processes, and the former constitutes a unique global organization while the latter constitutes a unique type of regional<sup>9</sup> organization,<sup>10</sup> this article will compare the normative initiatives on cybersecurity *sensu stricto* which the two organizations have undertaken.

The overall aim is to discuss how and to what extent global governance gaps on cybersecurity are being filled, by analyzing the most salient recent developments in cybersecurity law

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take responsibility for ensuring cybersecurity, leading to various legal and practical obstacles in regulating the issue.”

<sup>2</sup> Cybercrime can be defined as “a criminal activity in which computers or computer networks are the principal means of committing an offense.” Examples include “cyber-theft, cyber-trespass, cyber-obscenity, and cyber-extortions.” Some authors and instruments categorize cyberattacks against critical infrastructure under ‘cybercrime’. In this article discusses the EU NIS Directive [EU, 2016, *infra* Section IV), which aims to protect critical infrastructure regardless of whether a cyberattack against such infrastructure should be seen as falling under a strict definition of ‘cybercrime’. A specific regional instrument dedicated to cybercrime as such is the Budapest Convention on Cybercrime [Council of Europe, 2001]. See also the African Union Convention on Cyber Security and Personal Data Protection [African Union, 2014; Orji, 2018].

<sup>3</sup> For example, Rules 20–95 of the Tallinn Manual 2.0 [Schmitt et al., 2017].

<sup>4</sup> Many initiatives that aim at regulating cybersecurity only address a certain area of its framework, such as the protection of critical infrastructure (e.g. EU NIS Directive), data protection online (e.g. the famous European GDPR Regulation), cyber warfare (e.g. the Tallinn Manual 2.0). The definition or concept of cybersecurity used often varies according to the specific legal domain at hand [Kosseff, 2018, p. 985].

<sup>5</sup> E.g. the Council of Europe’s Convention on Cybercrime. So far, 64 States have ratified this convention, 19 years after its official adoption [Pupillo, 2018, p. 4].

<sup>6</sup> The ITU Plenipotentiary Conference held in Guadalajara, Mexico, 2010, approved the definition. See Kshetri [2016, p. 3].

<sup>7</sup> See e.g. the United Nations Office on Drugs and Crime (UNODC) Global Programme on Cybercrime, ITU Global Cybersecurity Index, UN Digital Blue Helmets, and the work within the Group of Governmental Experts on Information and Telecommunications Developments in the Context of International Security (“UN GGE”) (First Committee of the UN General Assembly).

<sup>8</sup> See e.g. the 2013 Cybersecurity Strategy, the establishment of ENISA (European Union Agency for Network and Information Security), the Cyber Defence Policy Framework (2014, updated in 2018), the development of cyber defence related projects under the Permanent Structured Cooperation (PESCO), the Joint Framework on Countering Hybrid Threats (2016), the Communication on Strengthening Europe’s Cyber Resilience System and Fostering a Competitive and Innovative Cybersecurity Industry (2016), and the 2017 Framework for a Joint Diplomatic Response to Malicious Cyber Activities (‘EU Cyber Diplomatic Toolbox’).

<sup>9</sup> In particular, one with supranational features [Schermer, Blokker, 2018, §60–61, 60–62].

<sup>10</sup> Calls have been made to regionalize cybersecurity regulation [Henriksen, 2019, pp. 5–7].

in the UN and the EU. First, on a more abstract level, the article will discuss whether international law can adequately regulate issues of cybersecurity: what impediments are encountered in regulating in the cyber domain? Vice versa, can the high-tech phenomenon of cybersecurity be embedded in international law? (II) The article surveys the work of the Group of Governmental Experts on Information and Telecommunications Developments in the Context of International Security (hereinafter: “UN GGE”), whereby the question arises whether its reports represent an emerging international *opinio juris*. (III) The problems associated with regulating cybersecurity at the UN level have led to calls for action at the regional level. In the EU, many policy initiatives in different subdomains of cybersecurity have seen the light of day. Two legislative measures stand out: the 2016 Directive on Network and Information Security (hereinafter: “NIS Directive”) [EU, 2016] and the 2019 EU Cybersecurity Act (IV) [Ibid., 2018]. The analysis thereof will allow one to discern whether and which impediments of regulating cybersecurity at the international level are shared at the EU legislative level (V). We conclude with some reflections on the desirability of regulating cybersecurity at the UN and EU levels. Are the difficulties of regulating cybersecurity embedded in the distinct lawmaking processes of the UN or the EU, or are they inherent to the phenomenon of cyberspace? At what level is cybersecurity regulation the most efficient, well-developed and promising? (VI).

## Cybersecurity and International Law: Strange Bedfellows

### ***Factors Explaining the Difficult Marriage Between Cybersecurity and International Lawmaking***

The difficult marriage between cybersecurity and international lawmaking can be explained by a number of factors [Tranter, 2007, p. 449].

#### *Fast and High-tech Cyber Revolution*

The digitization of the world is taking place at an unparalleled pace [Niemann, 2018, pp. 907–25]. It is expected that by the end of 2020 there will be more than 20 billion connected devices [Reuters Plus, 2018; Sandage et al., 2013, p. 1]. In contrast to how international lawmakers responded in a timely manner to certain developments in the twentieth century, such as the international law of the sea concept ‘exclusive economic zone’ (EEZ) [UN, 1982] and the protection of the seabed as ‘common heritage of mankind’ [UN, 1970], the cyber revolution is often said to be so fast and unpredictable that international lawmaking has difficulties catching up [Kittichaisaree, 2017, p. 336].

#### *Sovereignty, Territoriality, Fragmentation of Jurisdiction and Legal Attribution*

The core concept on which international law rests, State sovereignty, does not fit effortlessly with cyberspace [Vergne, Duran, 2014, pp. 126–139]. Although – thanks to the work of the UN GGE – there is agreement that the principle of State sovereignty applies in cyberspace [G20, 2015; Schmitt et al., 2017, Rule 1, p. 11; UN, 2013; 2015], no State can claim sovereignty over the entire cyberspace [Sandage et al., 2013, pp. 184; Schmitt et al., 2017, Rule 1.7]. The reason for this is that the many cyber infrastructures that make up cyberspace are located in different sovereign territories [Schmitt et al., 2017, Rule 1.7], and that in international law, territoriality allocates jurisdiction. Nonetheless, as Trachtman rightly observes, this fragmentation of jurisdiction should not be a reason to give up regulating cybersecurity altogether: after all, (cyber)conduct still occurs in a certain territory and effects are still felt in a certain territory

[Trachtman, 2013, p. 88]. Issues that transcend territorial jurisdiction are by no means new to international law (e.g. the law of the high seas, outer space, climate change). The challenge lies in the problem of legal attribution: it is often difficult to determine the identity or location of cyberattackers or their intermediaries [Kshetri, 2016, p. 7; Wheeler, Larsen, 2013, p. 1]. This is the true complicating factor according to Trachtman [Healey, 2012; Shackelford, Russell, Kuehn, 2016, p. 10; Trachtman, 2013, p. 88]: even when there are rules on cybersecurity in place, the legal attribution problem may weaken their effectiveness.<sup>11</sup>

### *Role of the Government versus the Private Sector*

A third factor that underlies the difficult relationship between cybersecurity and international law is the question of the (extent of the) regulatory role of the State versus that of the private sector in cyberspace [Groupe UMP, 2009]. Cyberspace is a domain in which industry and the private sector play a pivotal role. The private sector governs cyberspace in an informal manner, leaving less room for the formal legislator (the nation State) [Hoisington, 2017, p. 95]. The question then arises to what extent the State must or can impose legal obligations on the private sector while regulating cybersecurity. Vice versa, to what extent can cybersecurity regulation be effective if the private sector is not involved in its preparation and implementation? There are heated discussions about the role of the State as regulator in cyberspace. On the one hand, one can argue that the nation State has the obligation to enact legislation that regulates or restricts the private sector in its cyber activities. The argument here is that the State must uphold its legal obligations under international law, such as the protection of human rights, international peace and security, the customary 'no harm' principle [ICJ, Corfu Channel Case, 1949; Trail Smelter case (United States v. Canada (1938 and 1941)),<sup>12</sup> the protection of critical infrastructures [EU NIS Directive, 2016, *infra* Section IV], and so on. According to some, these obligations can only be guaranteed in the cyber domain if rights and obligations are imposed on private actors [Kittichaisaree, 2017, pp. 335–52]. On the other hand, some question whether the role of the State within the cyberdomain can and should be that far-reaching. The main arguments in favour of a limited oversight function of the State are: (i) the private sector does not have sufficient incentives to duly cooperate with the State since this could jeopardize its commercial objectives [Teplinsky, 2013, pp. 225–322] (i.e. reputation damage, counterattacks by competitors using released technology); (ii) regulation will slow down innovation [Contreras et al., 2013, pp. 1115, 1119]; and (iii) the private sector prefers a private legal system as opposed to public criminal law [Wall, 2007, pp. 25–6]. An alternative solution would be that the governance of cyberspace be observed on the basis of (binding or non-binding) codes of conduct originating from industry itself.<sup>13</sup> The two aforementioned views should not be seen as mutually exclusive [Trachtman, 2013, p. 90]: whether and to what extent the State should have a regulatory role in cyberspace depends on the specific conduct one wishes to regulate. The

<sup>11</sup> Fidler [2015] talks about this problem in the context of treaties on cybercrime when applied to protect critical infrastructure from cyber threats.

<sup>12</sup> ICJ 9 April 1949, Corfu Channel Case (United Kingdom v. Albania), *I.C.J. Reports* 1949, p. 4; Reports on International Arbitral Awards, Trail Smelter case (United States v. Canada), 16 April 1938 and 11 March 1941, 3 *UNRIAA*, pp. 1905–82.

<sup>13</sup> An example of such an influential code of conduct is the "NIST" (National Institute of Standards and Technology Cybersecurity) framework. As its proponents argue, this document "harmonizes consensus standards and industry best practices to provide a flexible and cost-effective approach to enhancing cybersecurity that assists owners and operators of critical infrastructure in assessing and managing cyber risk, as the standard for due diligence." NIST *inter alia* collaborates with the United Kingdom, Japan, Korea, Estonia, Israel and Germany. However, it has been observed that a disadvantage of NIST is that it is less well suited to protect enterprises from sophisticated and targeted cyberattacks [Shackelford, Russell, Kuehn, 2016, p. 42].

“institutional choice may begin with determining whether the issue at stake is best taken on by the market, by private firms, by the State government, or by international law.”<sup>14</sup> Interestingly, the European NIS Directive imposes obligations on certain entities in the private sector (*infra*, Section IV)<sup>15</sup>, acknowledging that cyberspace is a domain in which cooperation between the State and the private sector is often necessary.

### *Applying Existing Law versus Creating New Law*

Is it sufficient to apply existing international law to the cyber domain, or should new rules be created that are specifically designed to address this challenge? Hoisington points to three competing views: (i) cybersecurity is to be addressed by using existing rules and structures under international law; (ii) cyberspace is fundamentally unique and requires new legal rules and structures; and (iii) existing law can tackle the challenge of cybersecurity, but those elements that are incompatible with its uniqueness should be set aside [Hoisington, 2017, p. 87]. What has been done so far on the international plane largely reflects the first view: the UN GGE has declared that international law, including the UN Charter, applies to cyberspace (*infra*), whereas the Tallinn Manual 2.0 transposes fundamental principles of international law to cyberspace in general (notably Rules 1–24) and more specifically to cyberwarfare.

### *Cyber Mania*

Cyber mania is another phenomenon that complicates the relationship between international law and cybersecurity [Kshetri, 2016, p. 2; von Heinegg, 2012, p. 5]. While developments in the field of cybersecurity law *sensu stricto* have been limited, a considerable amount of academic attention and policy interest has been devoted to the specific issue of ‘cyberwarfare law’. According to O’Connell, the highly mediatized cyberattacks in Estonia (2007), the cyber incidents during the Russo-Georgian conflict (2008) and Stuxnet (2010) gave rise to this militarized image of cybersecurity law [O’Connell, 2012, p. 191]. The majority of cyber incidents indeed does not reach the threshold of ‘armed attack’ within the meaning of Article 51 of the UN Charter [ENISA, 2015]. In reality, cyber threats are more complex and diverse in nature and often target private companies [Second recital, Preamble of the NIS Directive; d’Elia, 2014, pp. 240–60].

### *Interim Conclusion*

Given these multiple challenges, it is perhaps less surprising that there currently exists no global convention in the field of cybersecurity *sensu stricto*. The UN initiative that comes closest is the work of the UN GGE. In the next section, we analyze the reports of the UN GGE and explore their legal relevance.

## The UN Group of Governmental Experts<sup>16</sup>

The issue of information security first featured on the UN agenda in 1998, when the Russian Federation submitted a draft resolution on the topic in the First Committee of the UNGA. The UNGA adopted it without a vote as Resolution 53/70 [UN, 1998]. Since 2004, the UN GGE has studied the threats posed by the use of ICTs in the context of international security and how

<sup>14</sup> Trachtman [2013], according to whom this choice reflects the “true meaning of subsidiarity.”

<sup>15</sup> A careful reading of the NIS Directive makes it clear that ultimately, it are the Member States that must ensure that providers of essential and digital services comply with the obligations set out in articles 14 and 16 of the Directive (security and reporting requirements).

<sup>16</sup> This article is up-to-date until March 2020.

these threats should be addressed. Its work addresses issues of international law, in parallel to discussions on existing and emerging threats, norms, rules and principles, confidence building measures and capacity building [OEWG, 2020f]. The UN GGE reports of 2013 and 2015 are the most important and impactful ones. In its consensual report of 24 June 2013, the UN GGE established that international law, and in particular the UN Charter, applies in cyberspace just like in the physical space [UN, 2013, Para 19]. This includes the rules on State sovereignty and the principles resulting from the notion of sovereignty. For example, a State has jurisdiction over ICT infrastructure on its territory, and the State is responsible for international unlawful cyber acts that can be attributed to it [UN, 2013, Para 20; Schmitt et al., 2017, Rules 1–13]. In its consensual report of 2015, the UN GGE put forward the following principles of the UN Charter and international law as applicable in cyberspace to state behaviour: “sovereignty, sovereign equality, peaceful conflict resolution, the prohibition of the use of or threat of violence against the territorial integrity or political independence of a State, respect for human rights and fundamental freedoms and the principle of non-intervention in the internal affairs of other States” [UN 2015, Para. 28b]. This transposition to cyberspace of the fundamental principles of international law, which almost all constitute binding customary international law and/or have been confirmed by the International Court of Justice, is subject to a fairly broad consensus.<sup>17</sup> Several States, including certain ‘cyber superpowers’, had since confirmed the applicability of international law in cyberspace in their comments to the UN GGE reports and in their national cyber security strategies [République Française, 2018, paras 82, 85 and 87; Australian Government, 2016, paras 7, 28 and 40–41; Government of the Russian Federation, 2016, para 34; U.K. Government, 2016, para. 63]. This applicability was equally confirmed by the G20 in 2015 [G20, 2015, §26]. At that point in time, the UN GGE 2013 and 2015 reports could be seen as an indication of a growing consensus on the matter, and as evidence of the development of a certain *opinio juris*, which is one of the elements needed to eventually generate customary international law [Wouters et al., 2018, pp. 149–52].<sup>18</sup> Note that in the cybersecurity domain, State practice is largely classified and “partly contradictory” [Väljataga, 2018, pp. 4–5].

However, in June 2017, during the fifth meeting of the UN GGE, any meaningful development of *opinio juris* came to an abrupt end. Fundamental differences between the 25 members emerged, mainly on the issue of self-defence and on applying international humanitarian law to cyber conflicts. The Cuban delegation refused to recognize the explicit reference in the text to the applicability of the right to self-defence in cyberspace. According to the delegation, this would “legitimize an ICT war” [Soesanto, d’Incau, 2017]. The Cuban, Russian and Chinese delegations suggested the development of an entirely new set of international regulations and the creation of a UN General Assembly Working Group that would be open to all States, where ‘transparency, exclusivity and participation are central to discussion and decision-making’. The U.S. interpreted this as undoing all earlier progress made within the UN GGE [Bowcott, 2017]. As seen above, the 2013 UN GGE report confirmed the applicability of the UN Charter to cyberspace, and with this *implicitly* article 51 UN Charter, which concerns the right to individual and collective self-defence of a State. The same goes for the 2015 UN GGE report.<sup>19</sup> The Cuban

<sup>17</sup> These fundamental principles are reiterated throughout the Tallinn Manual 2.0 as being ‘black letter rules’ applicable in cyberspace; Henriksen [2019, p. 4].

<sup>18</sup> See also UN [2018c, Draft Conclusion No 9 and Commentary]; Haggemacher [1986, p. 5]; Bederman, [2010]; and Bradley [2016]. Note that the UN GGE is of limited membership, but the 2013 and 2015 rounds did include what are understood to be the most powerful cyber nations, such as the U.S., U.K., China and Russia.

<sup>19</sup> The UN GGE 2015 agreed on the applicability of the principles of international humanitarian law in the following terms: “The Group notes the established international legal principles, including, where appli-

argument was thus not so much legal as it was political. At the end of the 2017 session, no consensus report was adopted. By the end of 2018 the UN GGE was seemingly defunct [Bowcott, 2017; Henriksen, 2019, pp. 6–13; Soesanto, d’Incau, 2017].

In December 2018, though, agreement was found in the UNGA to establish two distinct processes in order to discuss the issue of security in the use of ICTs during the period of 2019–2021. With Resolution 73/27, sponsored notably by Russia [Ruhl et al., 2020], the UNGA established the Open-ended Working Group (hereinafter: “OEWG”), to the delight of the Cuban and Chinese delegations [UN, 2018a]. Eleven days later, the UNGA endorsed the commencement of the work of the sixth UN GGE, which is now called the ‘UN GGE 2019–21 on advancing responsible State behavior in cyberspace in the context of international security’ [Ibid., 2018b]. This resolution was sponsored by the U.S. It is worth noting that, whereas the OEWG is open to all interested UN Member States,<sup>20</sup> the UN GGE for the period of 2019–21 consists of 25 selected Member States: Australia, Brazil, China, Estonia, France, Germany, India, Indonesia, Japan, Jordan, Kazakhstan, Kenya, Mauritius, Mexico, Morocco, Netherlands, Norway, Romania, Russian Federation, Singapore, South Africa, Switzerland, United Kingdom, United States, and Uruguay [Ruhl et al., 2020; UN, 2018b, Para. 3]. While the UN GGE 2019–21 addresses norms, rules and principles, confidence building measures and capacity building and how international law applies to cyberspace [Geneva Internet Platform, n. d.], the OEWG can further develop or change norms, rules and principles listed in Resolution 73/27, confidence building measures and capacity building, how international law applies to cyberspace, existing and potential threats, establishing regular institutional open-ended dialogue within UN and relevant international concepts for securing global IT systems [UN, 2018a, Para. 5]. It has pointedly been observed that “the GGE and OEWG’s overlapping mandates suggest that they could operate as a sum greater than the parts – but it is important to recall that the OEWG is the product of a Russian proposal designed specifically to substitute for the U.S. call for another GGE” [Ruhl et al., 2020].<sup>21</sup>

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cable, the principles of humanity, necessity, proportionality and distinction” [UN, 2015, Para. 28.d].

<sup>20</sup> Some see this as an attempt by Russia to include more countries which would support its interests in cyberspace. See Grigsby [2018], Iasiello [2019].

<sup>21</sup> These authors see a risk of competition or even conflict between the two processes, and contend that “the United States and its allies see the OEWG as a forum for new stakeholders to learn about and spread the extant GGE norms. Russia, in contrast, may prefer to revisit previous GGE reports under the OEWG and revise them to better align with its interests. And while the 2015 GGE agreed on the applicability of the principles of international humanitarian law, this position was not noted in the establishment of the OEWG.” See in the same vein E. Iasiello [2019]: “The OEWG met in mid-September 2019 and some of the larger issues such as international humanitarian law that had previously prevented consensus surfaced again. While States like China and Russia have pushed back on international humanitarian law in the GGE, the OEWG meeting showed more States like Egypt for instance would be more inclined to back that position by placing less emphasis on its importance than other areas. More importantly, States that had not been able to express their opinions in the GGE now have a vehicle to accomplish that. States like Iran have been able to submit written statements highlighting their positions on issues. The larger OEWG may be the preferred avenue for States like China, Iran, and Russia that share the same philosophies with regards to cyberspace. Moreover, the opening of discussions to any UN Member State enables these governments to push for their preferred issues like cyber sovereignty (and by extension all that comes with it such as the controlling of potentially harmful information) by gaining the backing from other, smaller States, that might not otherwise have a say in the state-limited GGE. More authoritarian or closed countries may find themselves supporting the positions of their Chinese/Russian counterparts for the same reasons. Considering this, it comes as no surprise that Western countries like Australia, the United Kingdom, and the United States voted against OEWG’s establishment.”

The tentative programme of work (2019–2021) for the two processes looks as follows.

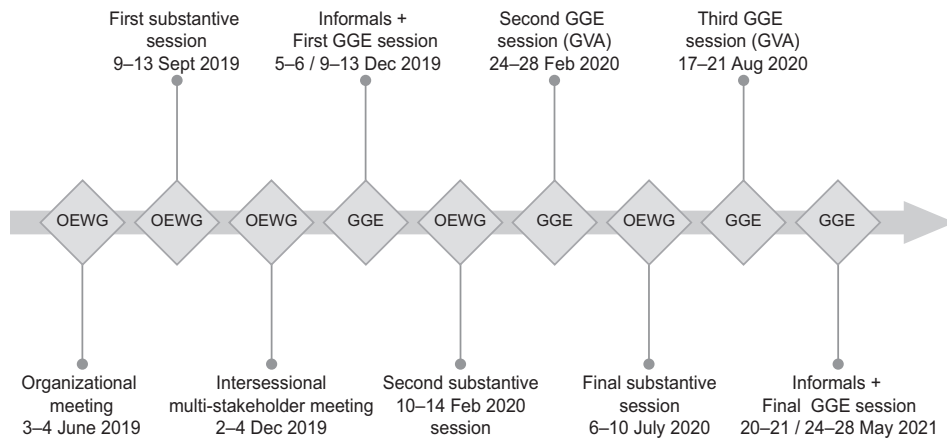


Fig. 1. Tentative GGE and OEWG “timeline” (2019–21)

Source: United Nations Office for Disarmament Affairs [n. d.].

Concerning the OEWG, the present article analyzed the publicly available documents of (i) the organizational session of 3–4 June 2019 [UN, 2019a; 2019b], (ii) the first substantive session of 9–13 September 2019 [UN 2019c; OEWG, 2019f], (iii) the informal multi-stakeholder meeting of 2–4 December 2019 [OEWG, 2019b; 2019c; 2019d; 2020a], and (iv) the second substantive session of 10–14 February 2020.<sup>22</sup> The analysis shows that the process is still very much in the stage of an exchange of views, with members discussing what the focus of the OEWG’s work should be. Members e.g. expressed that ‘the new (current) GGE and the OEWG should be mutually supportive and avoid contradictions’ [OEWG, 2020b]. The same can be said after analysis of the publicly available documents of the informal and first GGE session in December 2019.<sup>23</sup> This makes sense, as the OEWG is due to report to the 75<sup>th</sup> session of the UNGA, which takes place in the second half of 2020 [UN Office for Disarmament Affairs, 2019]. The UN GGE is due to report to the 76<sup>th</sup> UNGA session in 2021 [UN, 2018b, Para. 3].

While – especially in light of the more recent developments – it cannot longer be upheld that the UN GGE 2013 and 2015 reports represent an indication of a growing *opinio juris* of the international community, they nevertheless constitute an important indication of the applicability of international law to cyberspace. It remains to be seen if and what progress the OEWG and GGE processes will bring about, and whether these will result in a reaffirmation of certain principles, which could contribute to a development of an international *opinio juris*, or whether the outcomes of these processes, because of their political divides, will directly or indirectly conflict with each other and thereby neutralize any emerging *opinio juris*. Henriksen professed that the 2017 deadlock within the UN GGE would lead to more regional initiatives between like-minded States, such as at the EU level.<sup>24</sup> This is what the article now turns to.

<sup>22</sup> Non-exhaustively, OEWG [2019e; 2020b; 2020c; 2020d; 2020e; 2020f; 2020g]. See also the working papers submitted by Member States and informal papers submitted by intergovernmental organizations at the UN Office for Disarmament website [n. d.]. See Kaspar and Kumar [2019].

<sup>23</sup> At the time of submission, no documents of the second GGE session (24–28 February 2020) were available.

<sup>24</sup> According to Henriksen, the “regionalization of cybersecurity regulation into legal sub-systems of varying normative depth is unfortunate, given the global nature of the Internet.” At the same time, Henriksen ad-

## The EU 2016 NIS Directive and 2019 Cybersecurity Act

The EU has been vocal about its wish to play a leading role in cybersecurity [EU, 2018, Recital 15, Preamble]; EC, High Representative of the European Union for Foreign Affairs and Security Policy [2013, pp. 7, 11]; EC [2013a, p. 5; 2018, p. 1]; Westby, 2019; Fantin, 2019; Niebler, 2019.<sup>25</sup>

The NIS Directive is the EU's first ever horizontal and legally binding instrument on cybersecurity *sensu stricto*. It aims to protect critical infrastructure (essential service providers and digital service providers) from cyber incidents that have a 'actual adverse effect' on the security of network and information systems [EU, 2016, Art. 4.7]. The European Parliament and the Council of the EU adopted the Directive on 6 July 2016, which had to be implemented by 9 May 2018 in the national legal orders of the EU's Member States. The primary objective of the NIS Directive is "to guarantee a high common level of network and IT security" [Ibid., Fourth Recital, Preamble]. One of the main reasons for its adoption was that some EU Member States did not have cybersecurity legislation in place, and even when they did, there were large divergences among Member States. The EU's legislature was worried because 'cyber incidents are increasing in size, frequency and complexity and can result in business inability to do their jobs, significant financial losses to the EU economy and a loss of welfare for society' [Ibid., Second Recital, Preamble].

The NIS Directive imposes various obligations upon Member States, including ensuring a minimum national capacity by designating NIS competent authorities, by setting up computer crisis teams and through national NIS strategies and cooperation plans.<sup>26</sup> Interestingly, the Directive also imposes obligations onto two categories of private sector entities, namely the providers of essential services and providers of digital services.<sup>27</sup> The Directive sets out the

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mits that there are advantages to a more regional approach to cyber regulation, such as "avoiding time-consuming negotiations, the perspective of reaching agreement on complex issues rather than just on the low-hanging fruits," etc. See Henriksen [2019, p. 6]. In the wake of the 2017 UN GGE failure, US Homeland Security advisor Tim Bossart expressed that "it is now time to consider other approaches (...) and that the U.S. will work with smaller groups of like-minded partners." See The White House [2017].

<sup>25</sup> See also *supra* note 9.

<sup>26</sup> Each Member State must ensure a minimum national capacity by designating NIS competent authorities (art. 8 NIS Directive), by setting up computer crisis teams ('Computer Emergency Response Teams' – CERTs or 'Computer Security Incident Response Teams' – CSIRTs) (art. 9) and through national NIS strategies and cooperation plans (art. 7). National competent authorities must work together within a network (the Cooperation Group) that allows secure and effective coordination, including coordinated information exchange, and detection and response at EU level. Member States must exchange information and collaborate through this network to tackle NIS threats and incidents on the basis of the European NIS cooperation plan (Art. 11). One of the most important obligations for Member States is to identify the providers of essential services (Art. 5). A culture of risk management should be promoted (see recitals 4 and 44, Preamble NIS Directive) and the private and public sectors should cooperate and exchange information with each other. See EU [2016, Recital 35, Preamble], R. Roex [2016].

<sup>27</sup> The Directive focuses on two types of entities in the private sector (Articles 1, 4, 5, 14, 16): (i) providers of essential services and (ii) digital service providers. According to Article 5 (2) of the NIS Directive, providers of essential services are entities that 'provide services that are essential for the maintenance of critical social and / or economic activities, the provision of that service depending on network and information systems and in which in the event of an incident would have significant disruptive effects on the provision of that service'. In its Annex II, the NIS Directive specifies in a non-exhaustive way the sectors in which the Member States must search for the providers of essential services. These include the following sectors: banks, stock exchanges, transport and distribution of energy, air, rail and maritime transport, health, internet services and the government. Nuclear installations fall outside the scope of the Directive. See L. Lemmens [2018]. Digital service providers, the second private sector entity onto which the Directive imposes obligations, should be understood as online marketplaces, online search engines and cloud computer services. They are exhaustively listed in Annex III of the Directive. During the legislative process, it was decided that many of the other suggested digital services

following security and reporting requirements for providers of essential and digital services: (i) take appropriate technical and organizational measures to manage NIS risks; (ii) prepare and implement business continuity plans; (iii) notify the competent authority or CSIRT of an incident that has a significant impact on the continuity of the services they provide. What exactly constitutes a cyber incident with a ‘significant impact’ is thus quintessential to the implementation of the Directive, yet the meaning of this term is unclear at this stage<sup>28</sup> and it remains to be seen how this will be applied in practice<sup>29</sup>.

Secondly, one should point to the EU’s Cybersecurity Act, laid down in Regulation (EU) 2019/881 of the European Parliament and of the Council of 17 April 2019 on ENISA (the EU Agency for Cybersecurity) and on information and communications technology cybersecurity certification [EU, 2018]. The Regulation entered into force on 27 June 2019. The legal basis of the Regulation is art. 114 TFEU, which aims to further the objective of a properly functioning internal market as laid down in article 26 TFEU [EU, 2012; Mitrakas, 2018, p. 411]. The Cybersecurity Act has come about due to several factors, in particular the EU’s ambition to be a leader in the world’s cybersecurity market as well as its realization that the current framework is unable to quickly respond to certain threats, as evidenced by recent cyberattacks [Fantin, 2019]. Substantively, the Act introduces a pan-European cybersecurity certification scheme.<sup>30</sup> This should remedy the risk of market fragmentation<sup>31</sup> and should allow the EU to compete in the global cybersecurity arena [Mitrakas, 2018, p. 411]. The certificates will attest that a product or service meets certain evaluation criteria and provides for a warranted level of cybersecurity assurance [Ibid., p. 413].<sup>32</sup> An important obligation for Member States under the Act is to designate one or more national cybersecurity certification authorities in their territory or, with the agreement of another Member State, to designate one or more national cybersecurity certification authorities established in that other Member State to be responsible for the supervisory tasks in the designating Member State [EU, 2018, Art. 58.1]. In addition, the Regulation bestows upon ENISA, the European Union Agency for Cybersecurity, a permanent mandate and strengthens its role by providing it with more resources and by attributing further tasks.<sup>33</sup> Article 6 of the Cybersecurity Act stipulates that ENISA will assist Member States in their capacity building (e.g. in establishing and implementing vulnerability disclosure policies [Ibid., Art. 6.1(b)] and in developing national CSIRTs, making a direct link with the NIS Directive [Ibid., Art. 6.1(d)], although but note that the measures referred to in Art. 6 reflect best efforts obligations on the part of Member States.

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were not critical enough. See Roex [2016]. Under the NIS Directive, Member States are not required to identify digital service providers, allowing for a ‘catch-all approach’, see D. Markopoulou, V. Papakonstantinou and P. de Hert [2019, p. 4].

<sup>28</sup> Some guiding elements to determine what a significant effect is, are mentioned in art. 14.4 and 16.4 of the NIS Directive.

<sup>29</sup> A careful reading of the Directive makes it clear that, ultimately, it are the Member States that must ensure that providers of essential and digital services meet the security and reporting requirements of Articles 14 and 16.

<sup>30</sup> With a view to creating a digital single market for ICT products, ICT services and ICT processes, as the Act in art. 46.1 itself posits. See the security objectives of European cybersecurity certification schemes in art. 51 of the Act.

<sup>31</sup> E.g. France had already developed its own security certification scheme; ‘Certification Sécuritaire de Premier Niveau’ [Mitrakas, 2018, p. 412].

<sup>32</sup> Note that the schemes are currently voluntary. After a four-year period, the European Commission will be in a position to impose certain mandatory requirements if it sees fit [Fantin, 2019].

<sup>33</sup> Fantin has said that with this, the EU now considers ENISA an important actor to turn to for advice on potential 5G procurement and rollout [Fantin, 2019].

## Cybersecurity and EU Law: Irreconcilable?

Above, the article identified five factors that explain the difficult relationship between international lawmaking and cybersecurity. It will now be scrutinized whether (some of) these difficulties are shared at the EU legislative level.

### *Fast and High-tech Cyber Revolution*

The fact that the cyber revolution is a fast and high-tech one is inherent to the concept itself, and thus present at both the UN and the EU level. Evidently, the regional and limited membership of the EU, the like-mindedness of its membership, the absence of great cyber powers from the negotiating table as well as the established legal instruments, competences and supranational features of the EU explain why the EU has somewhat less trouble in catching up with the speed of the cyber revolution.

### *Sovereignty, Territoriality, Fragmentation of Jurisdiction and Legal Attribution*

The fact that cyberspace has no territorial limits is inherent to the concept itself and thus present at both the UN and the EU level. Concerning the NIS Directive, seeing how a country's critical infrastructure is most often located within its territory (e.g. drink water systems, hospitals, railways) [EU, 2016, Annex II] and thus within its territorial jurisdiction, EU governments can in general protect it without necessarily relying on international law [Fidler, 2015, pp. 9–10], thereby being less subject to the problem of fragmented jurisdiction. This is similar for the Cybersecurity Act, of which Article 58 stipulates that “each Member State shall designate one or more national cybersecurity certification authorities in its territory or, with the agreement of another Member State, shall designate one or more national cybersecurity certification authorities established in that other Member State to be responsible for the supervisory tasks in the designating Member State. National cybersecurity certification authorities shall: (a) supervise and enforce rules (...) for the monitoring of the compliance of ICT products, ICT services and ICT processes with the requirements of the European cybersecurity certificates that have been issued in their respective territories (...); monitor compliance with and enforce the obligations of the manufacturers or providers of ICT products, ICT services or ICT processes that are established in their respective territories (...)” [EU, 2018, Art. 58.1, 58.7(a), (b)]. Nevertheless, as seen, the more fundamental issue here lies in the more fundamental issue here lies in the legal attribution problem. This problem is also present at the EU level, and may equally weaken the effectiveness of its cybersecurity rules.

### *Role of the Government versus the Private Sector*

The fact that cyberspace is informally governed by the private sector poses a problem to regulators at both the EU and UN levels. In the NIS Directive, the EU legislature acknowledges the importance of imposing not only obligations on the Member States' authorities, but also on the private sector, notably the providers of essential services mentioned in Annex II of the Directive and the providers of digital services mentioned in Annex III of the Directive. The EU has the experience, legal tools, and internal market competences to do so. While the NIS Directive and the Cybersecurity Act allow Member States to lay down the rules for penalties in case of infringement [Ibid., 2016, Art. 21; 2018, Art. 65], this is no guarantee that the private sector has a sufficient incentive to duly cooperate with the State at the possible expense of its commercial objectives, nor that the regulations will not slow down innovation. It also remains to be seen how EU Member States will interpret a ‘cyber incident

with a significant impact on the continuity of essential and digital services,' and whether they can effectively ensure that operators of essential services and digital services notify the competent authority or CSIRT of such incidents [Ibid., 2018, Art. 14.3, 16.3], without which a lot of the measures of the NIS Directive are rendered meaningless of the NIS Directive are meaningless.

### *Applying Existing Law versus Creating New Law*

The NIS Directive and the Cybersecurity Act are examples of new rules being created after cybersecurity emerged as a policy problem. The political momentum in the Union, an organization with far-reaching legislative powers, to take a geopolitical direction on the matter plays a significant role.

### *Cyber Mania*

Cyber mania posing less of a problem at EU than at UN level requires little further explanation. The EU does not have the same mandate nor membership in the field of international peace and security as does the UN; neither does the UN have the same mandate in the field of economic policy and internal market and competition as does the EU.

### *Legal Binding Force*

As any EU regulation, the Cybersecurity Act has been binding in its entirety across the EU ever since it entered into effect on 27 June 2019.<sup>34</sup> As any EU directive, the NIS Directive is legally binding as well.<sup>35</sup> Portraying the legally binding force of these measures as a success to the detriment of UN efforts on cybersecurity would, however, be misleading. It is not particularly difficult to explain why consensus on legally binding measures could be found on this topic within the EU. Apart from the evident reasons (legal tools available to the EU, competences, supranational features, like-minded group argument), the NIS Directive introduces measures to protect critical infrastructures, a concept well defined in EU law [EC, 2005, Annex 1, p. 20; EU, 2008, Art. 2(a)] and at the forefront of international concerns in cybersecurity discussions [European Commission, 2005; 2009; 2013b; Melzer, 2011; UN, 2004]. The NIS Directive and the Cybersecurity Act were developed in the framework of the EU's longstanding and well-established competence to legislate on the internal market.

For now, it seems that almost all factors which hamper international cybersecurity regulation are inherent to the cybersecurity concept. They are therefore present both at the global and regional level and complicate the normative processes of the UN and the EU, however distinct they are. From this it should not be derived that regulation of cybersecurity *sensu stricto* should exclusively be done at either the UN or the EU level. The EU itself stated very recently, in the margins of the second substantive session of the OEWG, that "[t]he EU and its Member States support further engagement with key international and regional partners and organizations as well as with civil society, academia and the private sector in this field *with the aim of avoiding duplication of effort* [red.], and *looking for opportunities for synergies and burden-sharing* [red.], in order to support coordination and coherence in our collective efforts" [EU, 2019, authors' emphasis].

<sup>34</sup> Art 288, Para. 2 TFEU: "A regulation shall have general application. It shall be binding in its entirety and directly applicable in all Member States" [EU, 2012].

<sup>35</sup> See Art 288, Para. 3 TFEU: "A directive shall be binding, as to the result to be achieved, upon each Member State to which it is addressed, but shall leave to the national authorities the choice of form and methods" [EU, 2012].

## Concluding Remarks

This article identified five factors explaining the slow emergence of a global governance framework for cybersecurity, underlying the difficult relationship between cybersecurity and international law. They include the high speed at which global digitization is taking place as well as the nature of cyber operations; the fragmented jurisdiction and legal attribution problem; the question whether and to what extent the State and/or the private sector should have a regulatory role in cyberspace; whether transposing existing international law to the new technological context suffices; and the phenomenon of ‘cyber mania’.

The EU has managed to issue two legally binding acts on cybersecurity *sensu stricto*. It remains to be seen how and if the obligations in these acts are effectively implemented and complied with.<sup>36</sup> The legally binding force of the NIS Directive and Cybersecurity Act should not make one conclude that the UN’s work on cybersecurity has been a failure. Indeed, as is well-known in international law, soft law can be more effective than one might assume [cf. Boyle, 1999, pp. 901–12; Pauwelyn, Wessel, Wouters, 2012, pp. 159–60; Reisman, 1988, pp. 373–7; Virally, 1983, pp. 166–327; Wouters et al., 2018, pp. 165–7]. The work of the UN GGE between 2004 and 2017 made clear that international law applies to State behavior in cyberspace and brought together those States that actually are most engaged in cyber operations (China, Russia, U.S.). Yet, the UN GGE ran into troubles in going from the *whether* to the *how* [cf. Henriksen, 2019, p. 2]. At this moment in time, the UN faces a real risk that the splitting up into two processes – with the current GGE and the OEWG – will make overall agreement less likely, and drift further away from an international *opinio juris*. Regulating cybersecurity is stalled more because of politics than because of law at the UN level, whereas the current geopolitical momentum at the EU for regulation is high. In any case, advocating to exclusively regulate cybersecurity *sensu stricto* at either the UN or the EU level is a false dichotomy. Rather, synergies and cooperation should be sought. It would be highly regrettable if this proved impossible due to political rivalries and contestation.

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<sup>36</sup> Not only for the legal reasons we identified in this article, but also out of potential policy weaknesses. See e.g. C. Ducuing [2019, p. 23–4], D. Albrecht [2018, pp. 1–6] and to a lesser extent D. Markopoulou, V. Papakonstantinou and P. de Hert [2019, pp. 1–11]. See also Mitrakas [2018, pp. 411–14], Pupillo [2018, pp. 1–6] and Fantin [2019].

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# Financial Markets: From the “Tragedy of Commons” to Balanced Regulation

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## Abstract

*Nowadays the global financial system faces a triple challenge: the threat of a new systemic financial crisis at both global and regional levels; difficulties of constant adaptation of existing financial business and regulatory practices to intensive technological innovations; direct and hidden consequences of excessive political influence on the financial system through sanctions and selectively applied practices for sanction purposes. Improving the quality of financial regulation will require deeper cooperation between regulators of leading economies and a proactive position of the financial industry, as well as the decentralization of financial regulation. However, it is unlikely that this will happen at the global level. Financial stability became a key goal of global financial regulation in the post-crisis period. We consider financial stability as the “tragedy of commons.” The article describes the main trends of financial markets regulation after the crisis: transformation of global financial architecture, anti-money laundering and counter-terrorism financing practices (AML/CT), financial sanctions. The article analyzes the existing failures of modern post-crisis financial regulation: credit crunch, reduction in the effectiveness of monetary policy, regulatory arbitrage, and increased compliance costs (AML/CT legislation, tax legislation, and the sanctions regime). In the future we expect simultaneous trends of harmonization and standardization of requirements in traditional sectors of financial markets (including traditional institutions of the shadow banking sector), but at the same time regulatory arbitrage will induce new financial technologies in order to reduce regulatory costs. The crisis triggered by the coronavirus pandemic in 2020 despite its non-financial nature will almost inevitably have a major impact on financial markets and their regulation. Possible steps to eliminate failures in the financial regulation system are proposed, including recommendations for international organizations.*

**Key words:** financial regulation; financial supervision; global governance; international financial architecture; financial regulatory failures; financial stability; systemic risk

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## Introduction

Outdated, inconsistent and technologically lagging financial regulatory practices are considered to have been one of the key causes of the Great Recession of 2008–09 and consequent losses to the global economy. In the context of widespread and inconsiderate market liberalization in 1990–2000, these practices led to an accumulation of multilayered risks. Since 2009, there have been systemic changes in global governance mechanisms, but tough financial regulation has be-

come both expensive and burdensome such that the effectiveness of traditional financial institutions has been reduced. Today, the financial regulation system is being loaded with uncharacteristic functions, and governments are using financial regulation for law enforcement (though a growing network of anti-money laundering measures) and political purposes (via financial sanctions). As a result, the process of globalization and harmonization of financial markets has stopped, and regionalization processes have begun in certain market sectors. Banks and corporations have more limited access to capital, and non-market and non-financial considerations are increasingly used in financial decision-making. Under the conditions of over-regulation of traditional financial institutions, the development of shadow banking has been boosted.

After the Great Recession, financial global governance faced a serious challenge – the need to maintain a balance between the accumulation of systemic risk and the effectiveness of financial markets and institutions. In addition, technological innovations, changes in the approach to financial regulation and the increased impact on financial markets of compliance costs in the field of combating money laundering, terrorism, tax evasion and mutual sanctions have created additional opportunities and difficulties for regulators. These new factors increased the transparency of financial markets but significantly increased regulatory costs, destroyed existing business practices and, in many cases, reduced the coordination of actions of regulators and market participants. Thus, the collapse of the global financial system into separate components is the result of excessive regulatory burden.

Maintaining the integrity of the global financial system and developing well-coordinated financial regulation is a difficult task, despite reduced transaction costs and significantly simplified communication [Claessens, Kodres, 2014]. The demand for cryptocurrencies and the shift of financial activity from regulated areas to less regulated ones is a sign of significant structural and regulatory problems and the rigidity of regulatory practices.

In this article, we analyze prospects for regulating financial markets after the global financial crisis of 2008–09 using the concept of a common-pool resource. We consider the existing architecture of global financial regulation and its failures. In addition, prospects for regulating financial markets under the new global economic crisis caused by the coronavirus pandemic will be considered.

## Why Should Financial Regulation Be Harmonized?

Modern financial markets are highly interconnected, both across sectors and across countries. High integration leads to faster transmission of shocks and financial crises, and regulators are not always able to prevent an upcoming crisis.

A high level of capital mobility leads to increased volatility in capital flows. Both developing and developed economies are affected by this phenomenon: the instability of consumption, investment and exchange rate increases [ECB, 2016].

Financial stability is essentially a public good, or common-pool resource, so the state and international organizations must regulate and supervise financial markets at different levels to ensure smooth regulation and avoid major disruptions in their functioning. Today, because financial markets function at the global level, national governments cannot provide sufficient regulation and supervision, as evidenced by serious financial losses and increased destabilization of financial markets as a result of conflicting approaches to the bailout and bankruptcy of large investment funds in the U.S. and UK in 2008 and the ambiguous requirements for euro-zone banks in 2010–13.

Coordinated monetary, fiscal and macroprudential policies in different countries can reduce the volatility of capital flows. Uncoordinated macroeconomic policies, on the contrary,

can lead to negative external effects for other countries (especially developing economies) and increase vulnerability to financial shocks [Mohan, Kapur, 2014].

The lack of, or limited coordination between, regulators can lead to regulatory arbitrage, that is, the practice of transferring financial assets or certain transactions from a tightly regulated environment to a less regulated one. Regulatory arbitrage can occur between different sectors of the financial market or between different jurisdictions. As a result, risks accumulate in a poorly regulated environment, which threatens financial stability. The accumulation of huge off-balance-sheet liabilities on credit default swaps and the use of insurance companies that have fewer restrictions and requirements for transactions of this kind were significant factors in the collapse of Lehman Brothers and AIG. In the context of growing interdependence of financial markets, regulatory arbitrage has become easier and therefore more dangerous. In particular, there is empirical evidence that U.S. banks prefer to open subsidiaries in a less regulated environment [Frame, Mihov, Sanz, 2020]; the share of the shadow banking sector increased significantly over 2007–15, and at least a third of this increase was due to the additional regulatory burden placed on traditional financial institutions [Buchak et al., 2018]. Thus, requirements for banking and non-banking financial institutions, as well as requirements for financial institutions in different countries, should be as harmonized as possible in order to reduce the benefits of regulatory arbitration.

Harmonized regulation is particularly necessary for over-the-counter (OTC) transactions, which have historically been very poorly regulated due to the offshore nature of a significant part of this market. Without adequate regulation, cross-country regulatory arbitrage will occur with minimal obstacles, and financial assets will actively accumulate in a country with weak regulation or a “captive regulator” serving the interests of players of the regulated industry rather than the purpose of effective regulation. A crisis in one of these “financial casinos” will spread across the world economy very quickly due to the high interconnection of OTC markets. Some experts see the OTC market as a particular case of the “tragedy of the commons” that can be solved by internalizing costs [Coffee, 2014].

## Transformation of the Global Financial Regulation Model

Post-crisis strengthening of financial market surveillance coordination and financial regulation harmonization began at the Group of 20 (G20) summit in London in 2009. The summit decided to transform the Financial Stability Forum (FSF) into a permanent Financial Stability Board (FSB). The main purpose of the FSB is to coordinate the work of national financial authorities and international standard-setting bodies in order to promote financial stability.

The creation of the FSB was the first step toward establishing an *institution of financial stability* representing a set of rules and standards adopted to increase financial stability. Its infrastructure includes all international organizations that promote financial stability – the Bank for International Settlements (BIS), the International Monetary Fund (IMF), the World Bank (WB) and others. We believe that this financial stability institution is part of the global governance system.

The four main tasks of the FSB as the main coordinator for the financial stability institution are to build resilient financial institutions, end the “too-big-to-fail” problem, make derivatives markets safer, and transform shadow banking.

The BIS and the Basel Committee on Banking Supervision play a key role in solving the first two tasks – building resilient financial institutions and ending the “too-big-to-fail” problem. Basel III focuses on tightening capital, liquidity and leverage requirements, covering risk, and improving the stability of systemically important banks (international and national). The

International Association of Insurance Supervisors (IAIS) is also involved in improving the sustainability of financial institutions by developing the Insurance Capital Standard (ICS) and other supervisory standards.

The key player in achieving the last two goals is the International Organization of Securities Commissions (IOSCO). Together with the Committee on Payments and Market Infrastructures BIS, IOSCO has developed the Principles for Financial Market Infrastructures (PFMI) and recommendations for money market funds (MMFs).

In addition to implementing the principles of financial stability, the FSB constantly monitors the state of national financial systems. The joint IMF – World Bank Financial Sector Assessment Program (FSAP) exists for the same purposes.

The IMF's task is also to coordinate macroeconomic policies in different countries, but the IMF has very limited capacity to directly implement this task because the choice of macroeconomic policy is often a choice between national welfare and reducing external effects for other countries.

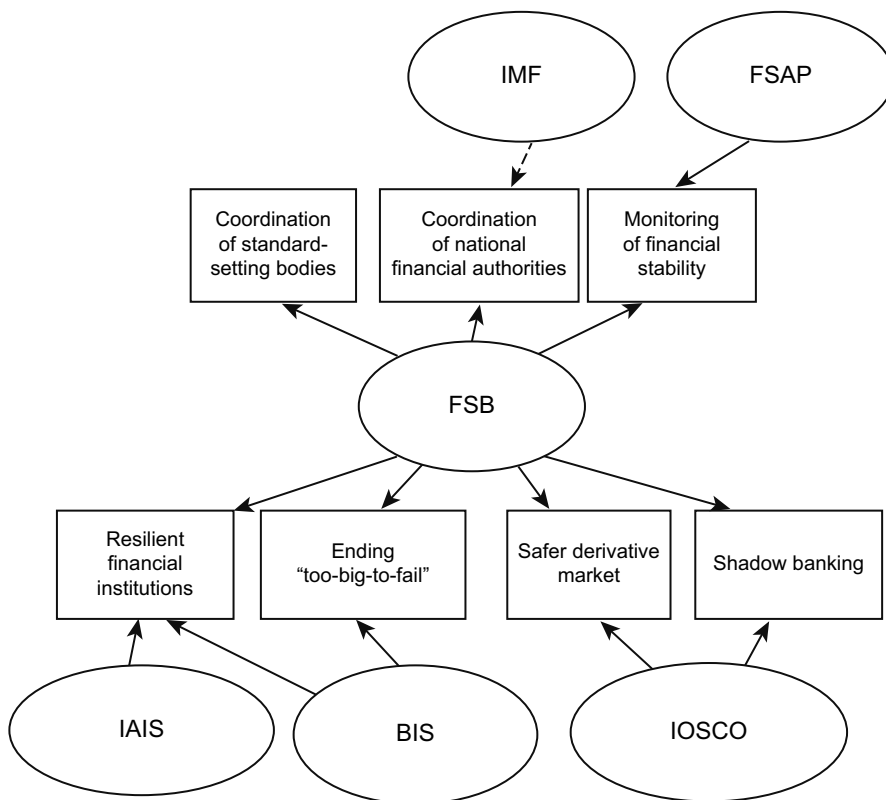


Fig. 1. Financial Stability Institution Structure

Source: Compiled by the authors.

According to the fourth FSB annual report on the implementation of financial regulatory reforms and their effects [FSB, 2018], a new institutional framework for financial regulation has been created over the years and major reforms have been introduced; the financial system has become more stable, but there are still elements of reforms that remain to be implemented.

Most researchers agree that Basel III had a positive impact on the stability of the financial system [IMF, 2018] both in developed economies [Gehrig, Iannino, 2017] and in developing economies [Hossain et al., 2018]. At the same time, economic growth has slowed due to the introduction of the Basel requirements. However, according to a new meta-analysis [Fidrmuc, Lind, 2018], the damage to national economic growth was less than expected: gross domestic product declined by only 0.2% in response to an increase in capital requirements of 1% per year.

According to the same FSB report, “good progress” has been made in the reform of OTC derivatives markets: trade reporting requirements, Central Counterparty Clearing (CCP) systems, margin requirements and capital requirements for derivatives that do not pass through the CCP system have been implemented. Moreover, the regulatory reform of OTC derivatives has had a positive impact on the volume and liquidity of the market. However, the reform is still being implemented, so it is not yet possible to assess the long-term effect.

Improving the stability of non-bank financial institutions is also not completed. IOSCO recommendations for money market funds are being implemented, and an incentive alignment regime for securitization is being introduced. The introduction of regulatory practices for shadow banking is at an early stage due to inconsistent definitions of this phenomenon and the lack of a legal framework, among other factors.

Thus, at present, changes in banking sector regulation are at an active stage and its elements are being rapidly implemented in different countries, while other sectors of the financial markets are receiving much less attention.

## Failures of the Financial Stability Institution

The financial stability institution is imperfect. There are a number of so called “failures” – situations in which the operation of the institution leads to an inefficient state, to a certain extent hindering the development of the economy. Among these failures are traditional regulatory failures, such as regulatory capture, failures caused by the operation of the institution itself (bias toward regulation of the banking sector), and failures associated with the implementation of new technologies.

Regulatory capture is a failure common to any regulatory practice, including financial regulation. This is a situation in which the regulator acts not in the public interest (to improve the efficiency of the economy) but in the interests of the stability and profitability of the regulated sector and begins to make decisions based on commercial and even extraneous (that is, political) considerations.

Regulatory capture is considered to have been an important factor in the global financial crisis, both at the national and global levels; after the crisis, the problem persists despite positive changes in global financial regulation [Baker, 2010].

Moreover, as discussed above, the set of measures to improve financial stability has a significant bias toward stricter banking regulation. At the same time, the derivatives market and shadow banking still fall under the minimum regulations. This bias creates three key problems. First, tough requirements for banks, along with high compliance costs [Deloitte, 2017], lead to a reduction in bank lending opportunities and, consequently, to a credit crunch by reducing the supply of loans under the low interest rates. After the global financial crisis, there was an abnormally long credit crunch – the recovery of credit and investment activity took seven years, from 2010–17. Second, the bank lending channel of monetary policy transmission was disrupted because of the credit crunch. The key mechanism of the bank lending channel is to influence the supply of bank loans by affecting deposits, but in the context of the Basel requirements, the effectiveness of this channel is reduced. The third relates to regulatory arbitrage (mostly

intersectoral but also cross-country). A significant part of banking assets and many financial activities (market making, derivatives trading) are shifting to the shadow banking sector. Many borrowers use alternative sources of funding: small businesses and companies with short-term financing needs use the opportunities of shadow banking, while large businesses move to the bond market to obtain long-term funding. Reforms to the OTC derivatives market also have side effects. Small companies have difficulty reaching clearing agreements and incur high regulatory compliance costs, so cross-country arbitration occurs [FSB, 2017a].

Another failure of the financial stability institution is the regulation of new financial technologies in general and cryptocurrencies in particular. Fintech blurs the boundaries between financial markets and reduces the cost of financial transactions and barriers to market entry. It is likely that a significant part of the financial services currently provided by the banking and non-banking financial sectors will be replaced by services using new technologies (machine learning, predictive analysis, decentralized networks, blockchain and others). For example, in 2019, Facebook tried to launch the Libra cryptocurrency as part of the Libra payment system but faced intense opposition. Jens Weidmann, the president of the Bundesbank and ECB board member, called on eurozone banks to fight Libra [Gordon, 2020]. The U.S. Congress and the European Commission also made claims. According to Bloomberg, in early 2020 Facebook decided to reorient the Libra payment system to work with various digital currencies [Light, Bain, Kharif, 2020].

Fintech is developing rapidly but the financial stability institution cannot respond to innovations in a timely and adequate manner. A report published in 2017 by the FSB states the following: “The Financial Stability Board has developed a concept that defines the scope of activities using financial technologies, as well as the potential benefits and risks to financial stability. This will provide the basis for future analysis and monitoring” [2017b]. In other words, the FSB has admitted its inability to keep up with innovations, and the situation has not improved over the past two years.

Thus, the structure of the global financial system is changing under the influence of tools that are supposed prevent a potential shock. However, the possible reaction of the global financial system to a possible shock is also changing as the system’s vulnerabilities are shifting [Knight, 2018].

Sources of financial instability, actions taken to address this instability, and the consequences are presented in Table 1 (positive consequences are highlighted in bold and negative consequences in italics; neutral consequences are not highlighted).

Many researchers and experts regularly criticize the governance within the organizations of the financial stability institution and their coordination. The non-governmental organization New Rules for Global Finance described the quality of global financial management as “inadequate, unsatisfactory.” The criteria for evaluation were transparency, inclusiveness, accountability and responsibility; the G20, the FSB, the IMF and the World Bank were evaluated. The same organization in the same year described the impact of global financial regulation as very limited, especially in poor countries. The European think tank Bruegel also claimed in 2014 that the G20 failed to establish an adequate financial institutional infrastructure [Véron, 2014].

The debate over the quality of global financial regulation continues. Some experts disagree with the characterization of regulation as unsatisfactory [Sheets, 2017]. Other experts only partially agree that financial regulation has a limited impact [Knight, 2018]. At the same time, the U.S., being the largest source of capital, has several separate, poorly coordinated financial regulatory bodies whose decisions have had global consequences. Either way, it is unlikely that this source of uncertainty will disappear.

Further harmonization of financial regulation practices and financial standards can be expected in the future. The bias toward the banking sector is likely to continue. In particular,

the implementation of the final elements of Basel III (detailed principles for assessing market, operational and credit risk) is perceived by the market as Basel IV [KPMG, 2018] due to the high potential costs for banks to implement additional requirements.

*Table 1. Sources of Financial Vulnerabilities, Actions and Consequences*

Source of Vulnerability	Actions	Consequences
Banking sector	Basel II, Basel III	<b>Financial stability has improved</b>
		<i>Credit crunch. Lower efficiency of the bank lending channel. Regulatory arbitrage (lenders and capital shift to the debt market and shadow banking sector)</i>
Derivatives	Increased transparency. Encouraging the CCP	<b>Reducing counterparty credit risks. Reducing systemic risk. Narrowing of spreads</b>
		<i>Compliance costs</i>
Shadow banking	Monitoring	Growth of the sector due to the reduction of the banking sector
Fintech	Analysis	<b>Lower transaction costs</b>
		Uncontrolled development
		<i>Unsupervised risk source</i>

*Source:* Compiled by the authors.

The high cost of regulatory compliance in the banking sector has to some extent displaced financial innovation in the less regulated shadow banking sector.

The model of global financial governance has significantly transformed with the introduction of a new institutional environment. Evaluating the effectiveness of the new model is difficult enough; we will never be able to say with certainty whether the financial system has become more resilient thanks to the work of this institution or in spite of it, or whether it has become more resilient to any particular shocks or to all of them. However, we can suggest some steps that will help improve the institution of financial stability in one way or another.

## Other Sources of Problems for Financial Markets

**Combating Money Laundering and the Financing of Terrorism (AML/FT).** Money laundering – concealing the origin of illegally obtained income, usually through transfers through foreign banks or legal businesses – has been considered a problem for decades. Since 2000, the global anti-money laundering system has gradually shifted the burden of proving illegal activities from law enforcement agencies to financial institutions.

The main actor in the global fight against money laundering is the Financial Action Task Force (FATF), formed in 1989 by members of the Group of 7 (G7) and currently including 36 countries and two international organizations. FATF is an international organization, the goal of which is to develop and promote international action against money laundering. Since October 2001, the FATF was also included in the fight against the financing of terrorism. The FATF is currently drafting international legislation and developing national legislative and regulatory reforms to combat money laundering and the financing of terrorism. To date, FATF has developed 40 recommendations related to money laundering and nine recommendations related to the financing of terrorism. Countries that do not fully comply with the FATF recom-

recommendations may be pressured by the organization, which may recommend that member countries end relations with the non-compliant country's financial and non-financial institutions (this is the case, for example, for North Korea and, to a lesser degree, Iran).

Multi-million-dollar fines for major banks (such as Deutsche Bank or Société Générale, as well as "cleaning up" the banking systems of Latvia and Cyprus) for violations of legislation and international agreements on ATM, as well as the potential revocation of the license, provide incentives for full compliance with the law. Financial institutions find it extremely necessary to avoid suspicion and reputational risks.

Emerging economies are also under pressure — agreements oblige them to introduce similar rules at the national level. As a result, the cost of compliance and the number of employees required have increased significantly, as well as the difficulty of obtaining financial services for clients using the know-your-client (KYC) practice: in accordance with FATF requirements, information about each client of a financial institution must be analyzed in detail; every suspicious transaction must be reported.

Another problem is the emergence of blacklists with millions of potentially toxic companies and individuals who cannot receive traditional financial services due to complex procedures. It is becoming a global problem as data exchange between organizations and countries increases. Procedures for mutual inclusion on blacklists and rehabilitation of their participants are still in the embryonic stage.

**Tax Evasion.** National tax authorities cooperate with each other to prevent tax evasion but the global exchange of tax data and the introduction of requirements for financial institutions to verify suspicious transactions are relatively new. In the United States, FATCA (Foreign Account Tax Compliance Act), the law on tax reporting on foreign accounts, was adopted in 2010 for this purpose. FATCA provides serious penalties for foreign financial institutions that do not report the financial activity of American clients. For foreign financial institutions that do not comply with strict disclosure requirements, a 30% U.S. tax is imposed on all payments from the United States. FATCA defines foreign financial institutions extremely broadly — all possible types of financial institutions outside the U.S. fall under the definition. Foreign financial institutions are required to report directly to the Internal Revenue Service.

Almost all countries have signed the FATCA agreement, including countries that are under U.S. sanctions. FATCA and similar laws have a very limited impact on tax collection efficiency but impose additional regulatory burdens and pressure on financial institutions: on average, the compliance burden is about 1.2% of a financial institution's assets [Belnap, Thornock, Williams, 2018].

**Sanctions and Countersanctions: A New Source of Costs and Regulatory Demands.** Financial sanctions — such as the ban on financial transactions — have a long history. They were actively used during the Cold War and involve pressure on other countries to change their policies. In recent years, the importance of sanctions has increased significantly. Both the European Union (EU) and the U.S. use a wide range of bans and restrictions against Iran, Russia and, to a lesser extent, other countries for actions unrelated to the financial sector. Sanctions are imposed unilaterally, but the choice of measures is not transparent and is poorly regulated, even between countries that impose sanctions.

In this situation, financial institutions are forced to adjust their business practices and risk-sharing decision-making processes to avoid not only prohibited transactions but also potentially toxic transactions in the future. This itself increases compliance costs and requires the creation of an expensive and slow-functioning internal infrastructure to deal with the regulator

in complex cases. At the national systemic level, alternative infrastructures (such as payment systems) need to be maintained or created to avoid possible impediments to financial flows.

Such violations (real or expected) and uncertainty increase costs for business and regulation, even in jurisdictions that are not directly sanctioned. For example, Chinese banking institutions are experiencing difficulties due to anti-Russian sanctions. To comply with the sanction regime and national requirements, regulators and Chinese banks block and cancel Russian transactions, close bank accounts and delay the payment verification procedure. In accordance with U.S. requirements, sanctions must be imposed on every company with at least 50% participation of the person or company under sanctions. Also, sanctions should be imposed on every individual or legal entity that “was aware of and facilitated a significant transaction for or on behalf of one of the sanctioned individuals.” Assessing the risk of approving a Russian transaction for Chinese banks is difficult – it requires additional resources and knowledge of the Russian market and affiliations. In this situation, of course, Russian banks and companies are primarily affected, but there are losses on the Chinese side too.

## The Impact of the Coronavirus Pandemic on the Regulation of Financial Markets

In the first quarter of 2020, the World Health Organization (WHO) announced a coronavirus pandemic, which led to a downturn in the economy at the time of writing and will lead to a global economic crisis in 2020 and possibly 2021.

The probability of a banking system collapse is low. On the one hand, regulation of the banking sector has increased its resilience to various kinds of shocks, while on the other hand, in March 2020, central banks around the globe announced the easing of monetary and regulatory measures aimed at providing financial markets with abundant liquidity. Ultra-low or negative interest rates significantly reduce costs of servicing debt. Such rates are observed in all markets of developed countries, while in emerging markets rates are historically low and receding.

The credit cycle of developed countries is likely to return to a period of credit crunch. Under the lower rates on government debt, yields on corporate bonds and loan rates have increased both in relative and absolute terms (outside of special government programmes to support businesses). Artificial restriction of demand due to the imposition of measures against the spread of the epidemic and the forced shutdown of economic activity will cause significant damage to small- and medium-sized businesses and large companies of various sectors. In conjunction with the policy of near-zero or zero interest rates, it will increase the degree of credit crunch and complicate overcoming this state after the crisis.

In government support programmes, including concessional loans, credit resources will be rationed, not through interest rates or risk assessment, but through non-financial instruments. A side effect of a viral recession (“pandecession”) could be a radical increase in the share of the state and its agents in the credit market, even in those countries that managed to avoid this in 2008–10.

The probability of deoffshorization of national economies increases. Withdrawing capital from offshore will lead to a more even distribution of risks in the economy, reducing the number of high-risk assets in “financial casinos.” The volatility of capital flows between developed and developing economies is also likely to decrease.

The pace of fintech development will increase. The industry is almost guaranteed to benefit from the crisis, and its recovery has already begun. According to a study by deVere Group, the use of financial applications in Europe increased by 72% in the last week of March [2020].

## Ways to Modernize Financial Market Regulation

**Decentralization of Financial Regulation.** Small economies with developed financial markets do not have enough incentives to resist systemic risk, because they can benefit from regulatory arbitrage and at the same time avoid large losses if a financial crisis occurs. As mentioned earlier, financial stability is a common-pool resource, so there is a “tragedy of the commons.” Nobel laureate Elinor Ostrom has proven that small groups can manage resources efficiently and sustainably. Perhaps two-party or group agreements (if the group size is small) can work successfully not only for pastures but also for financial markets.

In contrast to the multilateral approach to financial regulation, agreements between a small number of countries can be reached and updated much faster, which means that they can respond to innovations in a timely manner. The jurisdictions that will be most affected in the event of a financial crisis should take a proactive position and formulate requirements for a particular financial market. In this case, these countries will be able to insist on extending these requirements to other jurisdictions directly or through organizations of the financial stability institution.

Ostrom also formulated the necessary conditions for the stability of such agreements: clarity of the law, unambiguous decision-making procedures, and rules for conflict resolution [2015]. Therefore, the financial stability institution should play a serious role in this process by creating a transparent institutional environment.

Thus, in the current institutional framework, financial regulation in small groups would be effective. One example of such a small group is the Eurasian Economic Union (EAEU).

*At the moment, the EAEU is working on the concept of a common financial market, which involves the gradual harmonization of legislation in financial markets of EAEU states (including the harmonization of requirements for financial market participants, the creation of a single exchange space and the creation of a single supervisory authority). The banking sector, which dominates the institutional structure of the financial markets of EAEU members, was chosen as the priority sector for the first stage of the formation of the common financial market. However, it is expected to develop a common approach to regulating all sectors of the financial market, up to the regulation of cryptocurrencies.*

The pandecession further contributes to the decentralization of financial regulation. Closing borders as part of measures to reduce the spread of the virus will reduce the volatility of capital flows and reduce the degree of regulatory arbitrage. However, opening borders may trigger a new wave of capital movements, so harmonization of financial regulation remains necessary.

**Self-Regulation.** Self-regulation is one of the most effective elements of regulation in financial markets. A self-regulating organization (SRO) is a non-profit organization that unites industry participants and is able to respond more quickly and effectively to changes in financial market practices or the external environment. Setting standards and requirements that are appropriate to existing business practices will ensure that such requirements are met at a higher level. The state regulator must ensure a balance between supervision of SROs and a certain freedom of action for them to work effectively.

The creation of international SROs for the largest participants in financial markets will ensure effective financial management at the micro level.

*One example of a successful international self-regulatory organization is the International Swaps and Derivatives Association (ISDA). The main goals of the Association are to reduce coun-*

*terparty risk, increase transparency in the relevant financial market sector, and improve the institutional environment in the OTC derivatives market. The Association has developed standardized terms for OTC swaps and derivatives contracts, which are successfully used by more than 900 market participants from 71 countries.*

**The Financial Regulatory Sandbox.** The “sandbox” is a special legal regime established by the financial regulator for testing financial innovations in a controlled environment. The main goal of the sandbox is to find a balance between reducing risks, suppressing economic growth, regulatory compliance costs, and protecting consumers’ rights in new, mostly financial and technological business models. The first financial regulatory sandbox was created in the UK in 2016 to support disruptive financial innovation [FCA, 2015]. To date, more than 25 countries have created or are planning to create similar sandboxes.

Financial regulatory sandboxes can help improve communication between the regulator and firms implementing financial innovations to establish an optimal legal regime for such firms. Moreover, financial regulatory sandboxes encourage operation and innovations of fintech companies in financial markets.

When economic activity is restricted or suspended as part of the response to the coronavirus pandemic, it is important to avoid suspending regulatory sandboxes as much as possible (at the time of writing, no country has suspended sandboxes).

**Regulatory Technologies (Regtech).** The rapid evolution of technology not only creates problems for financial regulation but also offers solutions. Modern technologies can simplify financial regulation in the context of regulatory monitoring, information provision and compliance.

A key area of focus for regtech today is compliance with the requirements of AML legislation and the KYC rule. In addition, regtech makes it easier for prudential regulation authorities to comply with disclosure requirements: the amount of information that needs to be disclosed every day is huge for a large bank, and modern technology makes it possible to automate this process. Thus, regtech allows for a significant reduction of the cost of disclosure and compliance.

Regtech will soon be able to eliminate the regulatory capture by implementing automated data access and automated data management and analysis. Perhaps in the future, regtech will allow for the setting of financial standards in accordance with a proportional approach, considering risk factors [Arner, Barberis, Buckley, 2017].

**New Sources of Capital.** Finding new sources of capital outside the EU and the U.S. may be a solution to problems for countries that are under varying degrees of sanctions pressure. New development banks are an example of such capital – they can help reduce the negative consequences of the sanctions regime in the future but at present they often make it difficult to effectively regulate the financial system.

**Reducing the Regulatory Burden on Pandecession.** The current economic crisis is of a non-financial nature, so there is no problem of moral hazard in helping banks – the crisis in the financial sector is not associated with excessively risky behaviour of banks or lack of regulation. Reducing the regulatory burden on the banking sector, along with other incentives for the financial sector, will help the economy recover from the crisis. This is also the position of the BIS: “banks should be part of the solution, not part of the problem,” said Agustín Carstens, director general of the BIS [2020].

## Conclusion

Regulatory practices in the last decade, armed with new technologies, have developed remarkably, which can significantly reduce the level of risk for financial institutions. However, the absence of major financial shocks since 2009 is more a result of low interest rates and relaxed fiscal policies in major markets than an accomplishment of better governance. We are seeing major economies diverge in their approach to regulating financial markets while maintaining one common trend – rising regulatory compliance costs. For more than a decade, the media and public have viewed the financial sector not as a source of development opportunities but as a swamp that needs to be drained, leading to even greater concern about the potential risks of transactions that were considered routine a few years ago.

In the nearest future, it is likely that regulatory practices will gradually be coordinated and harmonized, as will the requirements of legislation to combat money laundering and the financing of terrorism, and financial standards for regulators and major institutions will be established. At the same time, technology will allow some sectors of financial markets to move away from regulation into unregulated areas of operation.

The pandecession will strengthen some trends – the credit crunch, harmonization of regulatory practices, and the development of fintech. Other trends will likely slow down – the pressure on the banking sector will ease, and the problem of combating money laundering and terrorist financing most likely will lose priority status.

There is a set of measures that can help regulate financial markets more effectively. The first is continued harmonization of rules and practices by proactive regulators and greater reliance on modern technologies and self-regulation. The Basel requirements are one of the directions. Another step, which will require the cooperation of large institutions, is the unification of standards for evaluating clients and creating client profiles that can be transferred to different markets. Standardization can allow far more efficient use of huge data flows.

Second, methods of dealing with distressed financial institutions that created significant problems in 2008–09 and during the Greek debt crisis in the eurozone should be unified. Systemically important, too-big-to-fail banks and investment companies must not only comply with additional capital requirements but also, in the event of a systemic crisis, methods of working with such organizations must be coordinated. In the context of an economic crisis of a non-financial nature, the pressure on systemically important financial institutions should be relaxed and coordinated.

Third, modern technologies make it possible to improve the approach to risk assessment, and thus it would be effective for financial institutions to rely on independent risk management tools, such as rating agencies, to identify problem areas. However, in this case, additional measures should be applied to protect the independence of such instruments.

Finally, creating alternative infrastructure to reduce the impact of sanctions – although this is likely to be a difficult process – or creating more transparent and specific rules for setting them will help reduce the risks for financial institutions and their clients.

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# Assumptions of the Global Economic Crisis and Its Inception in the Spring of 2020 Due to the Covid-19 Pandemic

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## Abstract

*Think tanks, as well as international organizations, have identified significant threats to the development of the world economy, increasing the likelihood of a new global financial crisis in late 2020 – early 2021. The main challenges to the system come from trade wars that could lead to a crisis in the international system of trade regulation, a decrease in the effectiveness of public policy instruments, and a deterioration in the dynamics of global economic growth. An important factor leading to a slowdown in the global economy in 2020 will also be the coronavirus pandemic, although it is difficult, in the first half of 2020, to assess its final impact. The combination of these negative factors, coupled with the unresolved problems of the 2008 global financial crisis, significantly increases the likelihood of a new global economic crisis which could surpass the Great Depression of the 1930s. This study systematizes the main forecasts by international organizations and analytical agencies for the growth of the world economy and considers various theoretical concepts to identify the symptoms of the impending crisis. Ultimately, this article offers options for reducing the negative impact of the crisis on Russia. In connection with the coronavirus pandemic, preliminary estimates have been made of the likely damage to the world economy and the prospects for its recovery.*

**Key words:** Economic growth; global financial crisis; world economy; world trade; trade wars; theories of economic cycles

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## Introduction

In recent years, the expert community has been actively discussing the likely beginning of the global economic crisis in 2020–21. Imbalances in the global economy increase the probability of a global crisis. These imbalances include the trade war between the U.S. and China, the increased level of protectionism, political and economic problems in the EU, in particular,

related to Brexit, the slowdown in the Chinese economy. No one could say exactly where the “Black Swan” would come from. In late 2019 – early 2020, the concern of experts and the world community as a whole about climate change and environmental degradation has sharply increased. There was a strong belief that the failure to confront these problems would eventually trigger a global crisis.

However, these factors did not trigger the global crisis. Alarm signals from epidemiologists who warned of the threat of global pandemics after 2015 were almost ignored. As it turned out, the experts who warned about global pandemics were right. In the early spring of 2020, it became obvious that the cause of the new crisis is the coronavirus pandemic. The collapse in oil prices in March 2020 was an additional shock to the economies of many countries. Thus, the global economy was under a double blow. Published at the end of March 2020, forecasts suggested a serious reduction in global GDP by the end of 2020.

The expected fall in the economy in 2020 may be followed by a recession in 2021, and its consequences may be much more extensive and destructive than as a result of the global financial crisis in 2008. Many economists believe that the real causes of the 2008 crisis were not eliminated, and the countries’ debt obligations were simply “flooded” with money.

The experience of global financial crises has shown that in each period there are some common symptoms indicating the beginning of a new crisis. In particular, on the U.S. stock exchanges in 2019, the yields of short-term securities were higher than the yields of bonds with longer maturities. The presence of such a symptom for a certain period of time, according to past experience, indicates the likelihood of a new global financial crisis.

Various indicators of the economic crisis reflect the growth of negative expectations on the part of investors, which lead to a sharp downturn of the market. Based on the analysis of theoretical works, it is possible to identify other signs indicating the possibility of the beginning of the world economic crisis. Increasing political divisions, along with growing imbalances in the global economy, can exacerbate the impact of negative factors increasing the risk of a new global crisis.

This paper examines the main indicators that reflect the probability of a new economic crisis. The indicators are based on existing theoretical concepts and patterns identified during various crises. The history of crises demonstrates the indicators that predict the beginning of a new global crisis. This research analyzes theoretical concepts and empirical data.

The study consists of three main parts. The first part considers the main forecasts of international organizations and analytical agencies on the state of the world economy. In the second part, we systematize the main indicators which are then correlated with real data. This predicts the beginning of a new economic crisis. The third part examines the first negative effects of the COVID-19 pandemic.

## The Pre-Coronavirus Forecasts of International Organizations and Analytical Agencies for Global Economic Growth in 2020

The forecasts of international organizations and analytical agencies allows us to determine the main expectations of potential investors regarding the dynamics of the global economy in 2020 and beyond. Table 1 shows the forecasts of international organizations remained quite moderate in mid to late 2019, in terms of the growth of world GDP and world trade. All forecasts show the general growth of the global economy.

According to the IMF, in 2019 there will be a slowdown in global economic growth compared to 2018. Forecasts for different groups of countries are significantly different. The growth of the aggregate GDP of developed countries suggests a slowdown, while emerging economies, on aggregate, will increase the pace of economic growth compared to 2018. The IMF predicts that global economic growth of 3% will be the lowest since the global financial crisis of

2008–09. Trade wars between the U.S. and China are a key reason for the slowdown in global economic growth. According to IMF forecasts, the growth in world trade will not exceed the growth in world GDP and will be approximately 3.2% in 2020 [IMF, 2019].

*Table 1.* Systematization of Forecasts for the Development of the Global Economy

Organization/Company	Date of Publication	Predicted Growth of World GDP, %		Predicted Growth of World Trade, %	
		2019	2020	2019	2020
IMF	October 2019	3	3.4	1.1	3.2
World Bank	June 2019	2.6	2.7	1.5	2
WTO	October 2019	1.2	2.6	2.6	3
UNCTAD	July 2019	3	3.5	4	4,9
OECD	November 2019	2.91	2.94	1.2	1.6
Barclays	November 2019	3.1	3.2	N/A	N/A
Credit Suisse	November 2019	2.5	2.5	N/A	N/A
Goldman Sachs	November 2019	3.1	3.4	N/A	N/A

*Source:* Compiled by the authors on the basis of official data of international organizations and companies [IMF, 2019; World Bank, 2019; WTO, 2019; UNCTAD, 2019; OECD, 2019; Barclays, 2019; Credit Suisse, 2019; Hatzius, Struyven, Walker, 2019].

The World Bank's (WB) estimates, see Table 1, confirm the IMF estimates [World Bank, 2020]. The WB forecast, in our opinion, deserves special attention. Based on an analysis of trends in the economies of several dozen countries, WB analysts concluded that the new economic crisis could surpass the crises of 1998 and 2008 with devastating consequences.

The WB saw the main problem as a sharp increase in the debt burden throughout the world, in both the private and public sectors. In 2018, global debt amounted to 230% of global GDP [Meredith, 2020]. The reason for the increase in global debt was unfulfilled obligations of developing countries. For the period 2010–18 the ratio of debt to GDP increased by more than 2 times [Kudenko, 2019].

Moreover, in the period from 2010–19, the emergence of debt was associated with the economic policy of China [Kudenko, 2019]. Over the years, the ratio of outstanding obligations to GDP reached 255%. Their actual volume exceeded 20 trillion dollars. Recently, in the framework of the well-known China-2025 program, in order to gain access to the latest technology in the country, the mass purchase of Western companies was encouraged. This policy was ensured by providing opportunities to attract loans, which contributed to a significant increase in corporate debt. Debt growth was associated with the active development of shadow banking in China. By the end of 2019, the volume of shadow banking reached almost seven trillion dollars, in connection with which the IMF warned that this bubble could bring down the country's economy and launch a new Asian crisis, similar to the collapse of 1997–98 [Kudenko, 2019].

During 2019, the WTO lowered its forecast for world trade growth from 2.6% to 1.2% [WTO, 2019]. This decrease is also associated with trade wars and introduced by trade restrictions for certain groups of countries. The removal of these restrictions, and a focus on the priority of free trade, would have a positive impact on the growth of world trade, which would contribute to the growth of world GDP.

Uncertainty in trade, as a key negative factor, influencing global economic growth, is also highlighted by the United Nations Conference on Trade and Development (UNCTAD).

Trade conflicts reduce opportunities for world trade, which leads to imbalances in the global economy. As a result, UNCTAD believes that world production will grow significantly faster than world trade [UNCTAD, 2019]. This trend contains a real risk of overproduction in some sectors, which could also lead to a new global crisis.

The OECD also updated its macroeconomic forecast downward during the year. The main reasons for the slowdown in economic growth in the world are the same: increasing protectionism and Brexit. The November OECD forecast for 2019 predicted a decline in the growth of global GDP to 2.9% in 2019 and 2020 [OECD, 2019]. The aggravation of trade wars has a significant negative impact on the expectations of business and investors. As a result, the growth rate of investments and the volume of world exports are reduced. A slowdown in world export growth was also observed before the start of the new global financial crisis in 2008.

In addition to the forecasts of global economic growth until 2020, made by international economic organizations, individual banks and analytical agencies offer their own forecasting options. According to their estimates, the situation may be slightly better than predicted by international organizations. For example, Barclays estimates the decline in economic growth rates to only 3.1–3.2% in 2019–20, which is slightly lower than the growth rates observed over the past 20 years (the average value was 4.1%). The trend does not necessarily indicate the start of a new global financial crisis [Barclays, 2019, p. 5].

Credit Suisse has approximately the same point of view: the global economy growth at 2.5% in 2019–20. This prediction is modest but suggests a recession is unlikely [Credit Suisse, 2019, p. 16].

According to Goldman Sachs, it is possible to expect a significant slowdown in global economic growth in 2020. However, Goldman Sachs predicts significant growth in the U.S. economy. It is expected that the global economy will accelerate in 2020, compared to 2019 [Hatzius, Struyven, Walker, 2019].

These expectations for 2020 are low and are associated with the significant fluctuations in world trade and investment. The intensification of trade wars will have a significant negative impact on the growth rate of the world economy, which could bring a new world economic crisis closer.

Since the beginning of a new crisis may be associated with economic imbalances, their identification is an important source of information about the state of the global economy. For the correct definition of crisis indicators, it is advisable to identify the growing imbalances at an early stage.

## The Indicators of the Beginning of a New Global Financial Crisis

A global economic crisis is the result of growing imbalances in supply and demand and significant changes in investor expectations. The presence of such imbalances is evidenced by a number of indicators. It is advisable to analyze them, along with the analysis of various economic concepts, and to systematize the main phenomena, the occurrence of which reflects a high probability of a new economic crisis.

### ***Changes in the Yields of U.S. Bonds***

A key indicator of the beginning of a new global crisis is a change in the yields of short-term and long-term bonds in the U.S. [Samiev, 2019]. Long-term bond yields should be higher so that investors can implement long-term projects. A situation where the yield of short-term bond yields exceeds the yield of long-term bonds over a long period of time has always been a symptom of an impending crisis.

From the standpoint of economic theory and practice, the investor compares the expected returns of investments, including indicators of income and risk. Long-term investments are usually characterized by higher returns, however, the growth of uncertainty in the long run leads to expected returns growing in the short term. Due to significant fluctuations in the global economy, investors cannot forecast the profitability of their investments for long periods, and, therefore, the attractiveness of short-term investments increases. An increase in the duration of such a situation affects the behaviour of investors. They become more impatient, because, due to growing uncertainty, they cannot expect, with a sufficient degree of probability, to receive a higher income from investing in long-term securities. A paradoxical situation arises: short-term lending becomes more profitable than long-term periods. Thus, the excess of the yield of short securities, over long ones, can serve as an indicator of an approaching crisis.

If you look at the situation in the second half of 2019, then certain negative trends are obvious. On August 14, the yield on two-year bonds exceeded the yield on ten-year bonds by 1.2 basis points [RBC, 2019]. This indicated the likely start of a new global financial crisis. If you look at the latest available real data on the yield on U.S. government bonds, then there is a certain imbalance [Investing.com, n. d.]. The yield on annual U.S. bonds is lower than the yield on shorter-term bonds. In other words, certain distortions (imbalances) were observed in bond yields. This picture gives us reason to talk about worsening investor expectations.

### ***A Decrease in the Profitability of Logistics***

An important indicator of a decrease in business activity is a decrease in the profitability of operations related to transportation. The slowdown in the rate of economic interaction primarily affects companies engaged in organizing business interactions. The reduction in profits leads to a reduction in the entire sector, which affects the growth indicators of the entire economy.

A decline in demand for logistics services, which is a consequence of falling trade volumes and trade imbalances, can be considered as a pre-crisis indicator. A specific illustration of the significance of this indicator, can be considered the deterioration in the dynamics of FedEx shares at the end of 2019 [A2 Finance, n. d.]. The company has a wide client base but has shown a decrease in demand for its services and the ensuing decrease in profitability.

### ***The Problem of Limited Economic Instruments***

One possible symptom of economic turmoil is the weak performance of financial institutions. As Paul Krugman believes that the main problem is that we will not be able to come up with an effective response if the economy slows down. The region in which the crisis is most likely to occur is the Euro zone [Kto v Kurse, 2019].

The problem is that the reduction in opportunities to modernize public policy is associated with the relatively low indicators of economic policy, and in particular, with the key rates of central banks. If the key rate is high, a central bank may lower it in order to increase market activity. However, the possibility of using this tool is very limited in countries where the value of this rate is about 1%, because there is simply nowhere to lower it further. Another tool may be to reduce collateral requirements and to extend credit terms, but this policy does not take into account possible risks and leads to the emergence of bubbles in the market.

It follows from the above that countries that have not exhausted the possibilities of state regulation of the economy are in a relatively better situation. The decline in the ability of the state to stimulate the economy, especially by means of monetary policy, can also serve as an indicator of a crisis.

In recent years, a number of economies have been experiencing the problem of zero interest rates, which naturally has a negative impact on the ability of government policies to stimulate economic growth. The most important benchmark is the value of the key rate in the EU. In particular, the European Central Bank (ECB) continues to maintain negative interest rates on deposit operations (as of 18 September 2019 the interest rate was  $-0.5\%$ ) [ECB, n. d.], see Table 2.

*Table 2.* Examples of Rates for Deposit and Credit Operations of the European Central Bank

	Interest Rates for Deposits	Interest Rates for Credits (Marginal Lending Facility)
18 September 2019	$-0.50$	0.25
16 March 2016	$-0.40$	0.25
9 December 2015	$-0.30$	0.3
10 September 2014	$-0.20$	0.3
11 June 2014	$-0.10$	0.4
13 November 2013	0	0.75
8 May 2013	0	1
11 July 2012	0	1.5
14 December 2011	0.25	1.75

*Source:* Compiled by the authors based on data from [ECB, n. d.].

In the EU, there is a non-standard situation associated with the formation of negative interest rates for a long period of time. Negative interest rates demonstrate that the Central Bank is trying to minimize liquidity absorption operations by encouraging investment in the economy. Placing funds in the ECB at negative interest rates is not profitable, however, credit institutions still continue to use this mechanism. These trends in the monetary policy of the ECB demonstrate the likelihood of a decline in business activity in the EU.

### ***Theory of Tugan-Baranovsky***

Tugan-Baranovsky pointed out that the income received in the economy is distributed between consumption and saving [Tugan-Baranovsky, 1997]. Income directed to consumption is an incentive for producers to increase their output. Savings are directed to free capital and capital in industry. Capital in industry is investment in production, while free capital is placed using financial instruments. Free capital moves between different industries. In the case of capital accumulation in industry, its profitability decreases. A crisis occurs when the flow of free capital directed to industry runs out. The decrease in the amount of free capital is associated with a decrease in the profitability of its placement. This concept confirms the assumptions associated with changes in the yield of securities in the U.S. market. For the development of the real sector, it is necessary to obtain funds for a long period of time, however, it is difficult to attract such funds due to a decrease in the profitability over a long period of time.

### ***Cycles of Kondratiev***

Kondratiev developed a theoretical explanation for the dynamics of economic cycles [Kondratiev, 1989]. The cyclical nature of the economy depends on the level of technological development. The downward phase of the economic cycle is characterized by a depression in agriculture. Another of Kondratiev's empirical observations is related to the predominance of

stages in the development of the crisis. If we consider large cycles, the period of upward phases is marked by years of recovery, while the period of downward phases of large cycles is marked by a depression in economic development. This makes it possible to single out the presence of certain crisis phenomena in the field of agriculture.

This indicator also finds confirmation, if you look at the data on the balance of supply and demand of agricultural products, it becomes obvious that there are certain imbalances. According to the OECD, in recent years there has been an excess of production growth over consumption, which has a negative impact on the price of agricultural products [OECD – FAO, 2019].

### ***Perez' Concept of Technological Revolutions***

Perez had a significant influence on the development of the concept of long waves [Perez, 2011]. Perez notes the crucial importance of technological revolutions and financial capital for economic development. The economy is constantly changing technological solutions which cause changes in the socio-economic organization. Changing technological paradigms is not possible without changes in governance, education, and regulation. Perez identifies the periodization of technological revolutions, the last occurred in 1971 with significant development of IT. It is possible to say that the global financial crisis of 2008 can be considered as a turning point in the economic life of countries. Since technological systems change every 50 years, the onset of the maturity phase should occur in 2020–21.

The maturity phase is characterized by:

- *shortening the life cycle of emerging technologies*. In the current period, we can observe a reduction in the periods of appearance of new high-tech products. Reducing the period of high profitability of products leads to a decrease in the profitability of their production;
- *increasing social tension*. Rich people continue to make profits, but the poor lose income. This causes social tension in the society. These trends have been confirmed in recent years (for example, the “yellow vests” protest movement in France in 2019).

Reduced profits and increased social tension (which is likely to increase in the context of the coronavirus pandemic) will lead to the emergence of a crisis. Perez' concept is clearly confirmed by the periodization of crises presented in her research.

### ***Low Security of Credit Operations***

Minsky defined financial crises as the relationship between fluctuations in investment and the receipt of information [Minsky, 1986]. There are three categories of firms in the economy: stable firms, speculative firms, and Ponzi firms. Stable firms attract cash. They can pay both the loan body and its interest. Speculative firms accept credit and can pay back the loan body or the interest. Ponzi firms take out loans, but they cannot pay either the interest or the body of the loan. If they are unable to repay the money on the loans, they will refinance the loan. At the stage of recovery, this is quite easy to do, because lenders have low interest rates. The mechanism continues to work until there is some news that changes the expectations of creditors who increase interest rates. The result is the bankruptcy of Ponzi firms and some speculative firms. After the economy is compressed, the mechanism is repeated. An indicator of the crisis is excessive lending, which is not significantly secured.

If you look at the size of private debt-to-GDP ratios, then in France, Germany, the UK and the U.S., their value exceeds the actual size of GDP. A significant increase in private debt is observed in France in 2018 compared to 2013 (Fig. 1).

These trends show a significant increase in the probability of default, which may eventually lead to the instability associated with the growth of negative expectations of creditors. The

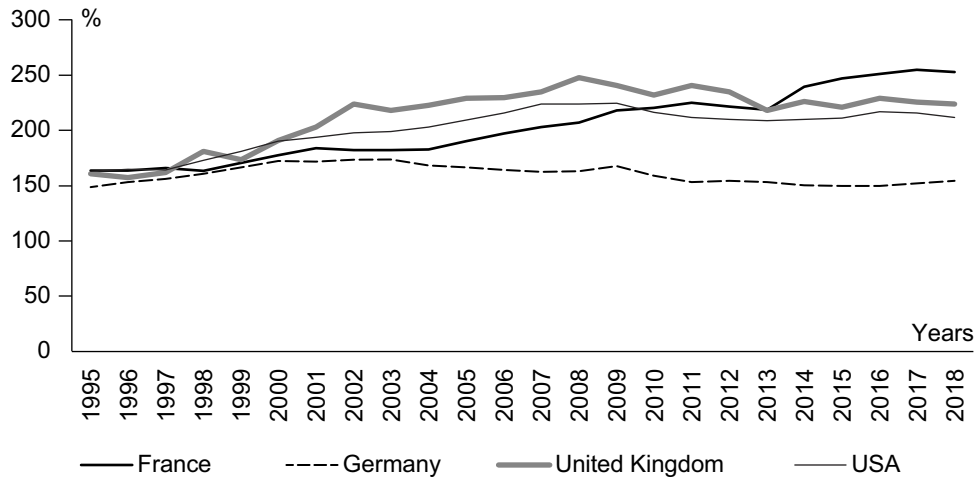


Fig. 1. Ratio of Private Debt to GDP, %

Source: The authors based on [IMF, n. d.].

probability of default on loans may be a significant indicator which demonstrates the possibility of a new global financial crisis in 2020.

The analysis shows that at the beginning of 2020, most of the indicators of the likely onset of a new global economic crisis are present in the world economy. These indicators are systematized in Table 3.

The most significant negative impact is the lack of real tools to stabilize the situation in the event of a financial crisis. Central banks are not all able to properly stimulate economic activity by reducing key rates. In this regard, it is possible to expect an increase in the role of mandatory reserve requirements. An important factor in the policy is insufficient collateral to attract loans. Given this development, central banks will have to expand the use of unsecured loans (which may lead to additional risks) and specialized credit instruments.

Factors not considered in international forecasts for the beginning of 2020 may include the coronavirus epidemic, which is likely to have a significant negative impact on the world economy. Reducing the negative impact can be expected if an effective vaccine against the virus is created. However, it cannot be excluded that over the next 12–18 months it will have a restraining effect on the state of the world economy.

Given the emergence of low interest rates in a number of countries and an increase in the number of deposits, there is sufficient free capital to ensure the growth of the world economy. In this regard, the lack of free capital cannot be considered as a source of the beginning of the global financial crisis. However, there may be a situation with the distribution of funds between speculative investments and investments in production. Potential crisis phenomena may be associated with changes in the expectations of economic agents regarding the prospects for economic growth. Examples of the implementation of negative expectations is the change in the yield of long-term and short-term securities and a decrease in the yields from logistics services, which can have a direct negative impact on business activity in the world economy.

For the first quarter of 2020, it cannot be said unequivocally that the onset of the global financial crisis is imminent. Obviously, investors have become more cautious [Kudenko, 2019].

Practically all well-known international agencies and authoritative experts predict the growth of the world economy in 2020 [MKRU, 2020]. At the same time, investor expectations and estimates remain quite cautious. Therefore, the possibility of a crisis cannot be excluded. Public

*Table 3.* Indicators of the Beginning of a New Global Economic Crisis

Indicator Name	Status at the Beginning of 2020	Brief Characteristic
Changes in the yield of securities in the United States	Occurs	Short-term bond yields exceeded long-term bond yields at the end of 2019
Coronavirus Pandemic	Occurs	At the beginning of 2020, the peak of the negative impact of the coronavirus epidemic has not passed. It is possible to expect a deterioration of the situation in terms of reducing economic interaction with China
The decline of profitability in logistics	Occurs	For some product groups, there is a decrease in revenue from transportation. The coronavirus epidemic in China also has a negative impact on this process
The limitations of economic instruments	Occurs	Some central banks have no real possibility of stimulating the economy in the event of a global crisis (for example, the ECB)
Reducing the availability of free capital (the theory of Tugan-Baranovsky)	Not observed	Low interest rates and structural liquidity surpluses demonstrate that there is sufficient free capital to invest
Imbalances in the development of agriculture (cycles of Kondratiev)	Occurs	In some areas of agriculture there is an appearance of imbalances
Technological revolutions in the concept of Perez	Occurs	There is an increase in social tension and a decrease in the life cycle of products created
Low security of credit operations	Occurs	In the global economy, there is an excessive level of lending, which increases the likelihood of defaults

*Source:* Compiled by the authors.

policies of countries should include measures to prepare for such a turn of events. The latter is particularly relevant for export-oriented economies, such as Russia.

## Preliminary Estimates of the Impact of the Coronavirus Pandemic on the Global Economy

By the beginning of the first quarter of 2020, the expert community did not yet have a clear opinion about the inevitability of the onset of the global economic crisis. A trigger that could bring down global markets was not yet visible. Many international agencies and reputable experts predicted global economic growth in 2020 [MKRU, 2020]. In turn, the World Bank, at the end of 2019, noted a significant increase in world debt, the total amount of which reached 246 trillion dollars. This fact had a negative impact on the expectations of investors, who, at the end of 2019, remained quite wary [Kudenko, 2019].

The beginning of the Covid-19 epidemic, in the first quarter of 2020, recognized by the World Health Organization (WHO) as a pandemic on March 11, was the trigger for the global crisis. Before the Covid-19 epidemic, WHO experts regularly spoke about the high probability of a pandemic at global level. The latter was associated with previous experience in controlling epidemics of SARS and MERS viruses, H1N1 swine flu, Ebola, etc. [Rodick, 2020]. However, the warnings of epidemiologists were virtually ignored.

As a result, even developed countries were not prepared for the pandemic, either in terms of sanitary and epidemiological, organizational and administrative, economic, or moral and political terms. An example of this is the United States, where the President, initially, strongly ruled out the spread of the epidemic in America, and a few weeks later, by the end of March, the country came out on top in the world rankings, in terms of the number of infected with corona-

virus and was forced to start accepting foreign aid. The coming socio-economic consequences became clear: the number of applications for unemployment benefits jumped, in early April, to a historically record level – almost 17 million people lost their jobs in the United States in three weeks [Romashenko, 2020].

Delays in testing and the introduction of quarantine exacerbated the situation in the EU countries, in particular in Italy, Spain, France and the UK. The PMI business activity index in the Euro area showed a record decline for the month from 51.6 in February to 29.7 in March [Normand, 2020]. Other countries, such as Taiwan, South Korea, Singapore and Hong Kong, halted the spread of the disease at the beginning of April 2020. The latter was achieved through effective monitoring of infection chains, as well as the introduction and enforcement of strict quarantine measures [Rodrik, 2020].

In March – April 2020, the first estimates of the possible economic consequences of the pandemic were made. As noted by OECD Director General, Angel Gurría, at the G20 virtual summit in March 2020, each month of isolation will cost a reduction of two percentage points in annual economic growth in developed countries, which will ultimately negatively affect a third of their GDP [OECD, 2020].

The expectation of an unprecedented decline in world trade, in 2020, was warned by the World Trade Organization. According to forecasts of WTO experts, a decrease in the volume of trade in goods may reach 13% by the end of the year, according to an optimistic scenario. The pessimistic scenario, in case of failure in the fight against the epidemic, implies a decrease in trade by more than 32% [WTO, 2020b].

The wide variation between the two scenarios is primarily due to the very nature of the current health crisis and the significant uncertainty in the global economy in the near future. The uncertainty of the scenario estimates is also due to the fact that it is impossible to exclude the appearance of other factors that are unknown yet, the impact of which, on trade flows, will be significant. For example, conditions in the credit market may be complicated, which will inevitably narrow down the possibilities of financing trade. As a result, according to WTO estimates, the decline in exports will be more than 10% in almost all regions. The largest decline will be observed in exports from North America and Asia. Significant damage will be inflicted on industries with developed value chains. The latter will be especially noticeable in the export of electronics and automotive products. The pandemic necessitated the introduction of restrictions on movement between countries, which has a significant negative impact on trade in transport and tourism services [Portanskiy, 2020].

According to the head of the WTO, Roberto Azevedo, the crisis that began has a significant difference from the crisis of 2008 and, even, from the Great Depression of the 1930s. The banking system has a significant amount of free capital that can support the sustainable functioning of the global economy. Despite the growing concern of economists, before the pandemic, the world economy showed steady growth. It was a pandemic, as the WTO head put it, that “cut the fuel supply lines to the economic engine” [WTO, 2020a]. The international community is faced with the task of restoring the “fuel lines,” which will enable us to move on to stabilizing the situation in the global economy. In order to realize an optimistic scenario, an effective government policy is needed to control the spread of the pandemic. It is also necessary to develop economic policy measures aimed at preserving jobs and business during a pandemic [Portanskiy, 2020]. Moreover, in no case should protectionist measures be introduced, leading to the emergence of new shocks for the global economy. It is through maintaining a policy of open markets that would help restore value chains, which would lead to the restoration of previous volumes of world trade and investment [WTO, 2020a].

By early April, developed countries had announced measures to support the economy in response to the pandemic. Thus, the EU finance ministers agreed on an anti-crisis plan to

save the EU economy, according to which, a record amount of €500 billion will be allocated to stabilize the situation in the light of the coronavirus pandemic. Of these, €300 billion will go to support the unemployed, as well as small and medium-sized businesses [Gazeta.ru, 2020].

In the U.S., at the end of March, Congress adopted a package of economic measures worth \$2.2 trillion. In addition to this amount, a \$350 billion salary protection program should be adopted [Voice of America, 2020]. In general, in the United States, the declared assistance to support the economy, in connection with the pandemic by the beginning of April, amounted to about 12.5% of GDP. Germany allocated a third of national GDP to fight the pandemic. In Russia, at the beginning of April, 1.4 trillion roubles were allocated to counter the negative impacts of the pandemic, which amounted to 1.2% of Russian GDP [Chevtaeva, 2020].

According to the data for April 2020, it should be noted that, in most countries, the tipping point that allows us to talk about reducing the negative impact of coronavirus on the economic life of countries has not been passed.

## Conclusion

Given the rapidly changing circumstances in the world at the beginning of 2020, the authors feel justified to present the findings in two main parts: (1) the result of the study of the different approaches utilized, at the end of 2019, to predict the beginning of a new global financial crisis, and (2), analysis of the estimated impact of the pandemic in the industry and the prospects of overcoming it.

1) The study showed that, by the end of 2019, some economic indicators already predicted the onset of the global crisis, while others did not. From this picture, it follows that the beginning of the global financial crisis was possible, for example, if a major actor, such as Lehman Brothers, went bankrupt in 2008. In the absence of such an event, the world economy had a high chance of avoiding the onset of a new global crisis, especially since most well-known international agencies and authoritative experts predicted growth in 2020. Nevertheless, there was a premonition of a global crisis, as evidenced, for example, by the noticeable tension in the mood of investors. No one, however, dared to give an answer to the question of where the “Black Swan” would come from, i.e. what would trigger the crisis.

The conducted research gave some grounds to believe that, at the beginning of 2020, there was an increased probability of a new global economic crisis in 2020 – early 2021.

Given that the consequences of the previous global crisis, in 2008, were largely “flooded” with money, the new crisis is likely to reveal all the old problems. As a result, its negative impact may be stronger and more destructive than all previous crises in the twentieth and twenty-first centuries. The solution of crisis problems, by re-crediting the economy, is unlikely to lead to the desired result, since the leaders of world economic development are faced with the need to modernize the structure of national economies. The situation is aggravated by increased protectionism in the trade policy of the United States, primarily, which resulted in a trade standoff between the United States and a number of countries, primarily China. The continuation of the U.S. – China trade war, given the weight of these states in the world economy, poses a real threat to world trade and the global economy as a whole and remains the most important potential cause of the global crisis.

For Russia, early identification of signs of an approaching global crisis is extremely relevant due to the high dependence on external factors, which caused a severe recession in the country, reflecting the problems on world markets in 2008–09.

As for Russia’s anti-crisis policy, it seems that it should include several main directions. In particular, it is necessary to continue forming funds that can be used to maintain the required

level of public spending during the beginning of the crisis. The second important element is the implementation of state policy aimed at developing domestic competitive production. The latter involves redistributing part of government spending to certain industries. The choice of such industries is the task of a separate economic study.

2) The real trigger of the global crisis was the outbreak of a new coronavirus, recognized by WHO on 11 March 2020. The first weeks of the pandemic showed that, even developed countries, starting with the United States, were unprepared for it, either in terms of sanitary and epidemiological, organizational and administrative, economic, or moral and political terms. The corresponding warnings of epidemiologists about the real danger of a pandemic, made after 2015, were actually ignored. Some East Asian countries have responded better to the pandemic – South Korea, Singapore, and Hong Kong seem to have managed to control the spread of the disease by early April 2020.

The first analysis of the likely impact of the coronavirus pandemic on the global economy and trade, conducted, in particular, by the OECD and the WTO, provided rough estimates of the possible consequences of the disaster. According to the estimates received, the world economy and trade are expected to fall significantly by the end of 2020, both in the case of an optimistic scenario (up to 10%) and in the case of a pessimistic scenario (about 30% or more). Considerable variation in numbers between scenarios is due, on the one hand, to the possibility of other, yet unknown factors with significant effects on production and trade, on the other hand, to the impossibility to assess the effectiveness of measures to combat the pandemic, to be taken by governments.

According to a number of authoritative sources, in particular the head of the WTO, Roberto Azevedo, the beginning of the crisis has significant differences from all previous ones, including the crisis of 2008 and the Great Depression of the 1930s by its very nature. The enforced isolation measures taken actually block a significant part of production and economic relations, both within and between states. Therefore, success in minimizing damage will be determined by the speed with which governments control the spread of the pandemic and the ability to choose the most rational future economic policies. The choice to introduce new protectionist barriers, under the guise of saving the national economy, which will eventually, inevitably, lead to new shocks for the economies, in addition to the existing ones, would be disastrous in the current circumstances. On the contrary, keeping markets open to international trade and investment would facilitate a faster recovery.

The crisis, associated with the new coronavirus pandemic, has caused a lot of assessments and opinions about the future of the global economy and the world as a whole, which can be divided into two groups: “the world will be different” and “the world will, basically, remain the same, where the existing trends will be consolidated.” But both will tend to see the coronavirus disaster as a confirmation of their own point of view, looking for the first signs of the future economic and political order they have long desired!

Those who wanted to see the expanding role of the state will receive a lot of arguments to believe that this crisis justified their beliefs. There may be talk about the inefficiency of the current system of global regulation, caused by WHO mistakes in the fight against COVID-19. In turn, experts, criticizing the public administration system, will also talk about the insufficient level of its effectiveness. The latter will ask for a change in approaches to global regulation, demanding the creation of a unified world health system that will increase the effectiveness of counteraction to future pandemics. Thus, in a number of areas, there will be strengthening of public administration, with the simultaneous development of the globalization process [Rodrik, 2020]. Thus, COVID-19 is unlikely to significantly change the main trends in the development of the modern world, but it may well accelerate it.

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# Trade Conflict Between the U.S. and China: What Are the Impacts on the Chinese Economy?

S. Park

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## Abstract

*A trade growth has slowed down in the global economy since the global financial crisis in 2008. It seemed to recover in 2017, but declined again since the Trump Administration in the USA posed trade protectionism in 2018 that led trade conflicts with its major trade partners such as Canada, China, Japan, Mexico, South Korea, the EU. Among these partners, the USA amended FTAs with Canada, Mexico, and South Korea by negotiations. It still negotiates FTA with Japan. However, the US government took a different approach to China in terms of tradethat is based on a hard line for setting high tariffs on Chinese import goods. China also responded with high tariffs on US import goods. As a result, the trade conflict started by criticizing each other, while the US represents its national interest first and China indicates the global free trade system as a key issue. In reality, the trade conflict has influenced not only the US and Chinese economy, but also the whole global economy negatively because the two economies as G2 accounted for nearly 40 percent of the global outcome. Therefore, it is one of the most sensitive issues on the global economic growth how it will affect to the global economy further. This paper argues why the trade conflict has emerged and how to solve it. It also focuses on economic impacts of the trade conflict on the global economy in general and Chinese economy in particular. Furthermore, it analyzes how the Chinese government deals with trade negotiations with the USA strategically.*

**Key words:** trade protectionism; trade conflict; economic impacts; Chinese economy; world economy

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## Introduction

The U.S. has been facing challenges due to the rise of China since China became the second largest economy in 2010. After the economic reform in 1978 named as the open policy, China's economic scale and foreign trade have been growing rapidly. As a result, Chinese economy surpassed German economy in 2009 and continuously Japanese economy in 2010 that was rather dramatic and very fast. China's role in the global economy has grown to be even more significant particularly since the global financial crisis (GFC) in 2008. It is widely recognized that the bilateral relationship between the U.S. and China will be a crucial determinant of the world's direction in the 21<sup>st</sup> century because China has tried to build a new form of cooperative platform in world politics and global economy by creating G2 in 2013. Since then, the U.S. and China started to open G2 Summit annually under the Obama government, but it stopped in the Trump government [Hsieh, 2009; Kirton, 2013; Park, 2017].

In order to play its roles properly in the global economy, China requested for additional voting rights in the International Monetary Fund (IMF) in the G20 Summit in 2009 that could increase its political and decision making power within the IMF. In 2016, the Chinese cur-

rency, Yuan, officially joined the Special Drawing Rights (SDR) basket and became one of the foreign exchange reserve currencies of the IMF along with U.S. Dollar, British Pound, Euro, and Japanese Yen. Furthermore, the quota of China in the IMF increased 30.5 billion SDRs in 2017 that increased from 1.8 billion SDRs in 1980. As a result, its total vote share increased to 6.09 percent. The currency composition of the SDR basket is reviewed every five years, and the current weights for the component currencies are U.S. dollar (41.73 percent), Euro (30.93 percent), Chinese Yuan (10.92 percent), Japanese Yen (8.33 percent), and British Pound (8.09 percent) [Momani, 2016; IMF, 2015].

Although the Chinese voting rights in the IMF are still weaker than those of the U.S. and the EU, its economic power has already been the second largest economy in the world since 2010. With the high economic growth of 6.6 percent in 2018, not only the U.S., but also the EU officially announced China as an economic competitor in the pursuit of technological leadership and a systemic rival promoting an alternative model of governance. The EU urged that China is no longer regarded as a developing country, but a key global actor and leading technological power. Therefore, China should take more responsibilities for upholding the rules based on international order and greater reciprocity, non-discrimination, and openness of its system. For it, China publicly stated reform must be carried out into policies, and actions commensurate with its role and responsibility [European Commission, 2019].

With the rise of China as G2, it is significant to understand the bilateral trade relations between the U.S. and China and the impacts of the two nations' increasing interdependence on the global economy. Several negative perspectives on the trade conflicts between the U.S. and China had been already expressed in the mid of 2000s. The major reason for the proliferation of trade conflicts between the G2 was based on the U.S.'s large trade deficit with China that may lead to a trade war between the two nations. The terms of trade war refer to an economic conflict caused by the fact that one nation imposes trade restrictions against the other nation promoting to retaliate by imposing higher tariffs or non-tariff barriers. As a result, it leads to a deterioration of bilateral trade relations [Stewart, 2006; Bezlova, 2007; Hsieh, 2009; Park, 2017].

Such a trend has continued through all U.S. presidencies and led to protectionism since the Trump Administration. The U.S. and China realized the trade conflicts as trade war although the both parties are negotiating to solve the trade conflicts. China has noticed fundamental changes of the U.S. government on Chinese political and economic power. The U.S. considers China as a serious threat to the U.S. global interests. It also rules out the possibility of China reforming gradually towards the Western system that resulted in a comprehensive review of past decades' US policy towards China. Accordingly, the core reason of the trade conflicts between the two nations is not only because of the economy, but also due to the politics in order to gain the global hegemony. It means that escalation of conflicts and confrontation is inevitable for the two nations in the long term perspective [Chin et al., 2018].

This paper argues when and why the trade conflict between the U.S. and China started. It also analyzes what may be impacts of the trade conflict between the two nations on the global economy as a whole and on Chinese economy in particular as well as how to solve the trade friction. Furthermore, it suggests how to prevent the possible trade conflicts based on protectionism in the future. In order to find answers of these questions, critical analysis of literature, inference and cross sectional analysis based on statistical data are employed.

## Theoretical Debates

Most of economists would agree with recent rebuttals to skepticism about the liberal trading order because of widely and rapidly spreading protectionism around the world. However, it is the fact that the intellectual and political support for free trade in the U.S. and elsewhere seems

to have been weakened since the GFC in 2008. At the same time, protectionism has started since then although G20 member nations agreed to prevent it at the G20 Summit in Washington D.C. Therefore, free trade based on multilateralism is regarded as a wishful thinking for many countries particularly in the U.S. since the Trump Administration [Hufbauer, Schott, 2008].

Economic theory suggested comparative advantage and economies of scale would create economic gains through economic efficiency. Therefore, tariffs led to competitive tariff retaliation, which result in a massive shrinkage in foreign trade and low global economic growth. Economic theory never urged that free trade is good for all industries and all people. However, the winners from the free trade can afford to compensate the losers and every one could be made better off because the aggregate gains are positive [O'Rourke, Williamson, 2001; Rosen, 2008].

Economic theory also says that resources will flow to more efficient uses. However, it does not apply when governments and markets do not work well. Therefore, Samuelson already urged in 1972 that the aggregate gains from trade are not necessarily positive for all nations. He expanded his idea further to claim that growth in the rest of the world can damage a country if it takes place in sectors that compete with its native exports having comparative disadvantage. As a result, relative and even absolute a nation's GDP per capita can fall in such a condition. Gomory and Baumol extended Samuelson's theory and urged that there is much possible equilibrium with vastly different outcomes for the countries involved in a modern free trade world. They stated further that it is perfectly possible or rather common for a nation's equilibrium trade outcome to be less than the self-sufficiency outcome. Accordingly, good equilibrium is often created rather than bestowed by nature. As a result, countries can do much to affect their trading outcomes. Therefore, they urge US protectionism in trade [Samuelson, 2004; Gomory, Baumol, 2009].

However, Bhagwati criticizes that Samuelson's explanation cannot be used as a justification for US protectionism. He also denies Gomory and Baumol's argument because the U.S. could not carry out effective industrial policies to remedy it although their argument is true. Krugman and Obstfeld support Bhagwati's critics that it is an empirical question rather than a fact whether the growth of emerging economies has actually hurt advanced countries although theoretical possibility still exists [Bhagwati, 2009; Krugman, Obstfeld, 2009].

Economists have developed theoretical models for free trade and estimated welfare gains from reducing or eliminating trade barriers. In line with these models, Krugman, and Broda and Weinstein suggested that trade benefits society through gains overall quality and variety. However, this standard static growth from the free trade has left trade promoters quite vulnerable because the static growth models consider only the short run partial equilibrium efficiency gains. At the same time, the static models generate the gains from trade range very marginal [Krugman, 1997; Broda, Weinstein, 2006].

In order to deepen theoretical models finding long term efficiency gains and contribution of free trade to economic growth, economists have developed dynamic models estimating impacts of trade liberalization used by cross country regressions. By using these models, Bradford et al. urged that the US economy in 2005 could generate higher economic growth than without post war trade liberalization. However, Acemoglu left the issue of trade and growth undecided because there are models that highlight both positive and negative effects of trade on economic growth so that empirical work must be conducted. Accordingly, Lewer and Van den Berg pointed out that further development of dynamic models and additional empirical research are required. Additionally, linkages between trade and technology as well as trade and institutional quality must be further developed [Bradford et al., 2006; Acemoglu, 2009; Lewer, Van den Berg, 2007; Feenstra et al., 2009].

In this paper, the dynamic models rather than static models can be adopted because the former can explain the long term benefits of the free trade more precisely than the latter. Ac-

cordingly, the conservative dualism of trade theory explains why the U.S. protectionism has emerged since the global financial crisis. It represents the Trump government trade policy than any other theoretical background. However, it has limited to generate the global economic growth sustainable. Therefore, it is possible that the dynamic models based on the long term efficiency gains and economic growth can correct the direction of protectionism toward the free trade. It is the reason why the U.S. and China have started the trade negotiation since 2018 and its outcome may be visible in the near future.

## Trade Conflicts Between the U.S. and China

### ***Background***

The large size of the trade deficit between the U.S. and China has been a significant issue in bilateral trade relations. The Trump Administration regards the trade deficit with China as a sign of unfair economic policies in China although the U.S. government has suffered from its chronic budget deficit since the 1980s. Therefore, it has reportedly request China to develop a plan to reduce the bilateral trade deficit targeting by \$ 100 billion. However, there is a large difference between the two nations' view on their official trade statistics. According to the U.S. trade statistics in 2017, the merchandise trade deficit with China accounted for \$375.3 billion, while Chinese trade surplus with the U.S. in the same year was \$275.8 billion. Nearly \$100 billion difference exists between the two nations that could cause a serious dispute between the two parties. However, a statistical working group established by the U.S. – China Joint Commission on Commerce and Trade (JCCT) in 2004 identified the causes of the statistical discrepancies that does not mean any error in the official statistics of either country [Martin, 2018].

In fact, the U.S. has had the largest trade deficit in the world over three decades since the 1970s. Exceptionally, the U.S. had briefly a trade surplus in the mid of 1970s, but has experienced continuous deficit since then. The U.S. deficit increased over 5 percent of the national GDP in 2005 and fell to 2.9 percent of the national GDP in 2017. Owing to the rapidly increase of the U.S.'s aggregate trade deficit, the Trump government criticized major U.S. trade partners generally and China in particular. The U.S. argues that China must correct its unfair trade policies generating huge trade surpluses with the U.S. that creates the trade imbalances between the two nations [Genereux, 2017; WTO, 2018; Park, 2018].

### ***Development and Current Situation of Trade Conflicts***

After a longer than six decades' free trade movement, the U.S. has recently shaken the foundations of the global trading system by imposing steep tariffs on imports from China and other major trading partners since President Trump took the power in 2017. The trade conflicts between the U.S. and other major trading partners in general and China in particular started as the US International Trade Commission (USITC) found that imports of solar panels and washing machines caused injury to the US solar panel and washing machine industries in Oct. and Nov. 2017 respectively. The two U.S. industries filed separate requests for the investigations in early 2017 under Section 201 of the Trade Act of 1974 that were the first industry petitions since 2001.

As a result, President Trump approved global safeguard tariffs on \$8.5 billion in imports on solar cells and modules and \$1.8 billion of large residential washing machines in Jan. 2018 that were imposed beginning on 7 Feb. 2018. As a counter measure, the Chinese government requested to have consultations with the U.S. under the WTO dispute settlement framework concerning these imports. Moreover, the Chinese government announced preliminary antidumping duties of

179.6 percent on imports of U.S. agricultural product, sorghum and imposed preliminary tariffs in April 2018. Chinese tariffs on US sorghum ended during negotiation in May 2018, and China also filed WTO dispute against U.S. solar panel tariffs in Aug. 2018. This signaled the significant trade conflict between the two parties that started the macroeconomic impact on the global economy negatively [Bown, Kolb, 2018; Ng, Chung, 2018; Bolt et al., 2019].

Moreover, the Trump Administration imposed tariffs on imports of steel with 25 percent and aluminum with 10 percent in Feb. 2018 under name of threatening the U.S. national security based on Section 232 of the Trade Expansion Act of 1962. Chinese portion covered only 6 percent of imports due to prior US imposition of antidumping and countervailing duties. Therefore, the Chinese retaliatory tariffs on this issue only accounted for \$3 billion. China also imposed tariffs on various imports from the U.S. that included 128 tariff lines.

In addition to steel and aluminum, President Trump imposed 25 percent tariffs on 1,333 Chinese products in two phases starting July 2018 that accounted for \$50 billion targeted intermediate inputs and capital products because U.S. Trade Representative (USTR) found that China conducted unfair trade practices related to technology transfer, intellectual property, and innovation that was investigated under Section 301 of the Trade Act of 1974. China also issued an updated \$50 billion retaliation list of 25 percent tariffs including agricultural and food products, crude oil, automobiles, airplanes, chemical products, medical equipment and energy products etc. in two phases that accounted for 659 tariff lines. Since then, trade conflicts between the two parties have continued, and President Trump directed the USTR to identify an additional \$200 billion of Chinese imports for additional tariffs of 10 percent in response of Chinese retaliatory tariffs in June 2018. The USTR finalized the tariff list containing 5,745 full or partial lines of the original 6,031 tariff lines that were on a proposed list of Chinese imports. The additional tariff was effective starting in Sep. 2018 [Bown, Kolb, 2018; McLarty Associates, 2018; Ng, Chung, 2018; USTR, 2018].

Since the additional tariff of 10 percent on \$200 billion of Chinese imports, the ongoing trade conflict between the two nations has continued. Amid the trade conflict, the U.S. government threatened to impose tariffs as high as 25 percent on all U.S imports from China if China implements its further retaliation measures. President Trump decided on increasing the tariffs to 25 percent on \$200 billion of Chinese imports in May as the trade negotiation between the two nations was not met. As a result, China also responded its retaliation measure to set the high tariff up to 25 percent on \$ 60 billion of U.S. imports. Due to the ongoing trade conflict, the neighboring countries of China such as Japan, South Korea, Thailand, and Vietnam suffer from a stiff decline of their exports to China although their exports to the U.S. increases at the same time. Additionally, China started to consider all options to strike back by targeting large-sized US corporations operating in China. It was announced after the U.S. government prepared more tariffs on imports of China and banned Chinese high-tech firm, Huawei [Bolt et al., 2019; Strauss, 2019; Cong, 2019].

During the trade conflict, the U.S. government has considered to raise the tariffs on all imports of automobiles and auto parts that could impact on the global economy massively. It could raise the risk of spreading the trade conflict at a global scale and escalating retaliation measures all over the world. However, the Trump Administration announced a delay of its final decision on whether to impose broad tariffs on automobile and auto part imports for about six months right after imposing the tariff of 25 percent on \$200 billion of Chinese imports. If the tariffs on all imports of automobiles and auto parts are realized, the U.S. major trade partners such as Germany, Japan, South Korea, China, Mexico etc. will be affected severely that could result in a global economic slowdown. In fact, the global trade conflict started due to the high U.S. trade deficit from China and other major trade partners. However, at the same time, the U.S. high tariffs imposing against the U.S. major trade partners in general and China in particular have intensified the global trade conflict further [Salama, Mauldin, 2019, table 1].

Despite the harsh trade conflicts, the two largest economies finally agreed the trade deal in Dec. 2019 and signed on it in Jan. 2020. It could change the economic relationship between the U.S. and China significantly. The agreement includes that China has committed to buy an additional \$200 billion of the U.S. goods and services by 2021 and ban on illegal business practices that the U.S. government has criticized. However, the accord does not provide information about how to work in practices. Therefore, it is possible that China could interpret text of the accord differently than the U.S. It is the reason why the second trade war between the two parties may be possible in the future [Eavis et al., 2020; Office of the United States Trade Representative & Department of Treasury, 2020].

*Table 1. Category and Content of US Trade Conflicts With Major Trading Partners*

Category	Content
Solar Panels and Washing Machine	Imposing safeguard tariffs on \$8.5 billion in solar panels and \$1.8 billion in washing machines. Chinese preliminary tariffs on US sorghum & filing WTO dispute against US solar panels tariffs. Korean filing WTO dispute against US solar panels and washing machines tariffs
Steel and aluminum as national security threat	Section 232 of Trade Expansion Act of 1962. 25 percent on steel & 10 percent on aluminum covering \$48 billion of imports
Unfair trade practices for technology & intellectual property (IP)	Section 301 of Trade Act of 1974. \$50 billion of 1,333 Chinese products for 25 percent tariffs with two phases. Identifying \$200 billion for 10 percent tariffs in Sep. 2018. Raising tariff to 25 percent on \$200 billion in May 2019
Auto vehicles as national security threat	Announcing to raise tariffs up to 25 percent and delay six months in 2019 mainly against the EU, Japan and South Korea

*Source:* [Bown, Kolb, 2018; McLarty Associates, 2018; Ng, Chung, 2018; USTR, 2018; Salama, Mauldin, 2019; Strauss, 2019].

### ***Reasons for the Trade Conflict Between the U.S. and China***

There are many reasons for trade conflicts whenever these take place regardless of between nations and regions. Among these, the trade conflict between the two largest economies can be explained with the following four reasons that are claimed by the two parties commonly and observed by the outsiders. These are trade imbalance between the two nations, US protectionism based on income inequality and chronic budget deficit, China's unfair trade against intellectual property right (IPR), technology transfer and innovation for US companies, and competition of hegemony power in the 21<sup>st</sup> century.

Firstly, the U.S. trade deficit with China accounted for \$419 billion in 2018 that increased from \$376 billion in 2017 although the Trump Administration imposed high tariffs on imports goods from China. The share of U.S. trade deficit with China in 2018 accounted for nearly 42 percent of the total U.S. trade deficit although it declined from 49 percent in 2015. The U.S. imported \$540 billion from China in 2018, while it exported \$120 billion to China in the same year. The three biggest categories of the U.S. imports from China were computers and accessories, cell phones, and apparel and footwear that accounted for \$77 billion, \$70 billion, and \$54 billion respectively. The three largest US exports to China were commercial aircraft, soybeans, and autos that accounted for \$16 billion, \$12 billion and \$10 billion respectively. It indicates that the U.S. trade deficit with China is not a short term based phenomena, but a long term based chronic trend due to the different industrial structures between the two nations. As a

result, the U.S. trade deficit increased from \$273 billion in 2010 to \$419 billion in 2018 continuously [Amadeo, 2019; Park, 2018; United States Census Bureau, 2019, fig. 1].

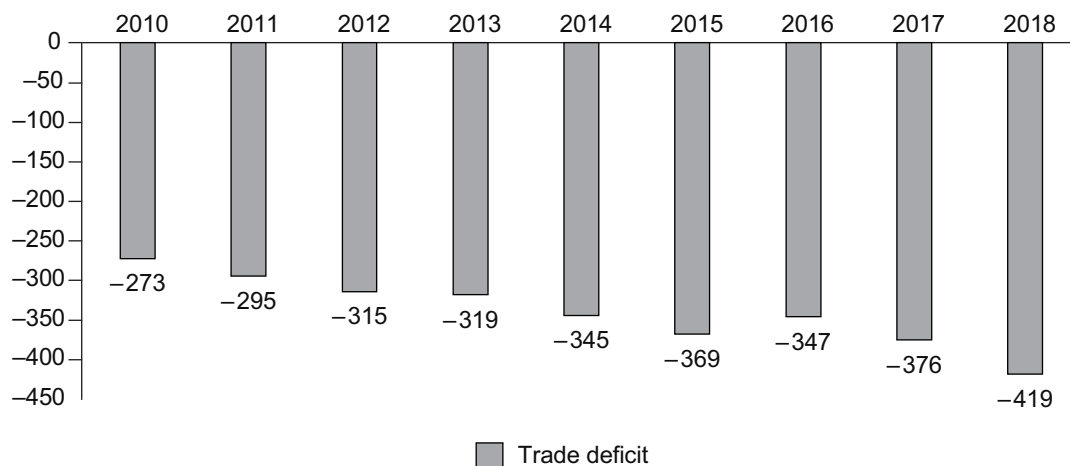


Fig. 1. The U.S. Trade Deficit with China from 2010 to 2018 (As of USD billion)

Source: [United States Census Bureau, 2019].

Secondly, the U.S. as the largest economy in the world has led to protectionism since the GFC in general and the Trump Administration in particular that has affected to the global economy severely. The U.S. protectionism impacts on the global economy negatively due to its economic size compared with other economies. It results mainly from the income inequality and distribution as well as a vast government budget deficit in the U.S. that has risen since the 2000s. However, economists are not sure yet whether the free trade has created the income inequality and the budget deficit or not. Some economists urged that the free trade affected only about 20 percent of increase in inequality in the 1970s and 1980s when the U.S. trade was mostly North to North. With the shift of trade relations to North to South, a more negative impact on the wage of low skilled workers in the U.S. took place since the 1990s. Whatever the cause of rise in inequality, the fact is that the average of real wage of production per hour has been stagnant since the 1980s. As a result, the wage increase in production has lagged behind the growth in real GDP per capita. Moreover, the share of pre-tax income in the top one percent increased from 10.5 percent in 1980 to over 20 percent in 2016, while its share of bottom 50 percent declined from 20.5 percent to 13 percent during the same period. It may have caused a lower tax revenue. As a result, it led the U.S. as the most inequality nation among the advanced countries based on Gini index that increased up to 0.41 in 2016 [Krugman, 2009; ERP, 2009; Hillebrand et al., 2010; OECD, 2014; Piketty, 2014; Alvaredo et al., 2017; World Bank, 2019, fig. 2].

Thirdly, President Trump asked US Trade Representative (USTR) to investigate whether Chinese laws, policies, practices that may harm US intellectual property rights, innovation or technology development in Aug. 2017 or not, and the USTR initiated investigation of China under Section 301 of the Trade Act of 1974. It found that China conducted unfair trade practices related to technology transfer, intellectual property, and innovation so that President Trump imposed 25 percent tariffs on 1,333 Chinese products in two phases starting July 2018 that accounted for \$50 billion targeted intermediate inputs and capital products. China also retaliated with an updated \$50 billion list of 25 percent tariffs including agricultural and food products,

crude oil, automobiles, airplanes, chemical products, medical equipment and energy products etc. in two phases that accounted for 659 tariff lines [Ng, Chung, 2018; USTR, 2018].

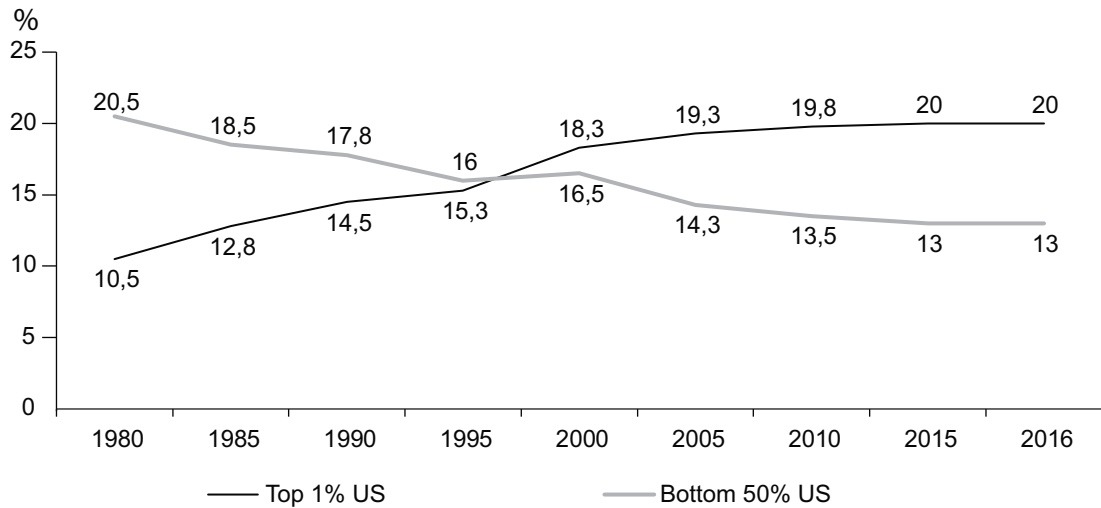


Fig. 2. Share of Pre Tax Income in the U.S. (As of 1980–2016)

Source: [Alvaredo et al., 2017].

Last, but not least the U.S. – China trade conflict is based on the competition of a hegemony power in the 21<sup>st</sup> century. Therefore, several scholars expect that it would take a long term instead of a short term. In the national security strategy report in 2017, the U.S. called China as its strategic rival. Additionally, the U.S. government particularly concerned the Chinese national development strategy, the Made in China 2025 program as a national threat in terms of high tech development that plays the core role in strengthening Chinese future competitiveness. In line with such a strategic point of view on the high tech area, President Trump signed on the executive order to ban the Chinese high tech firm, Huawei in May 2019 that is one of the leading global telecommunication companies in 5G technology in the world along with Ericsson, Nokia, and Samsung Electronics. The 5G technology is the key technology to realize the Fourth Industrial Revolution connecting the physical and cyber world. At present, China is one of the leading countries in this field ahead the U.S. that the U.S. government concerns mostly. If China succeeds the Fourth Industrial Revolution based on the 5G technologies, the U.S. technological supremacy will be over, and China will be the game changer in the world. Therefore, the key issue on the trade conflict between the two parties is rather politics than economics that escalate confrontation between the two nations continuously in the future [Schwab, 2016; The White House, 2017; Chin et al., 2018; Jiming, 2018; Doffman, 2019].

## Analysis on Impacts of the Trade Conflict

### **Trade Conflict and Tariff Measures**

Impacts of the trade conflict are not only bilateral, but also global. Particularly, the two largest economies in the world generate two fifths of global GDP and about a quarter of global trade. Therefore, the bilateral trade conflict between the U.S. and China is worrisome for both

the region and the world because the two nations are two of the three main hubs for global production chains along with the European Union (EU) with tight trade links in key industrial sectors such as electronics and high technology equipment [Abiad et al., 2018].

Most of the products affected in the first two rounds of bilateral tariffs imposed on imports of Chinese goods for \$50 billion are mainly capital and intermediate goods that are targeted for the Made in China 2025 plan. In order to meet the target of the plan, China needs to import high tech products for its end-products. These products are deeply connected with global value chains. By contrary, China retaliated to impose tariffs mostly on imports of the U.S. agricultural products, chemicals, medical and energy equipment. These products are rather homogeneous goods available in the global markets.

The second round of the trade conflict of \$200 billion by the U.S. and \$60 billion tariffs by China started in the mid of 2018 that affected to consumer goods because fewer supply chain lines were left to set the targets. The trade tension between the two nations escalated continuously, and the U.S. threatened to impose tariffs of another \$267 billion on Chinese imports. It was all goods imported from China in 2018. China also threatened to retaliate with similar tariffs on all imports from the U.S. It also considers other measures to retaliate the U.S. companies operating in China. In the global trade tension, the U.S. government has considered to set the tariff of 25 percent on imports of automobiles and auto parts from all trading partners that would affect \$350 billion worth of goods [Abiad et al., 2018; Park, 2018].

### ***Impacts on the U.S. and Chinese Economy***

The escalation of trade conflict and threats between the two nations caused a significant pressure of outlook for the global economic growth in general and the Chinese economy in particular. The Chinese export and sales started already weak in the third quarter of 2018. Additionally, the threats influenced investors in a wait and see mode and accelerated restrictions of foreign direct investment (FDI) for the high tech areas from China and vice versa [Hanemann, 2018].

In order to analyze impacts of the trade conflict on the two economies, it is reasonable to adopt studies of global research institutes providing objective and independent analyses, which are not influenced by the U.S. and China. One of these is the report of Asian Development Bank (ADB) that analyzes the implications of three scenarios. The first scenario is a current scenario including all trade measures implemented as of Oct. 2018 with \$200 billion of imports from China in 25 percent of tariffs. The second one is a bilateral escalation scenario intensifying to impose blanket tariffs of 25 percent on all merchandise imports from the both countries. Finally, the last scenario is a worst case scenario including measures under the bilateral escalation scenario and a global escalation of trade conflict between the U.S. and other trading partners in automobiles and parts imposed by the U.S. on 25 percent tariffs of imports from other nations (see table 2).

The immediate impact of these three scenarios will take time to be materialized fully. The current scenario will be affected fully in 2019, while the direct impact of the worst scenario will approach nearly a full effect in 2020. The worst scenario could be completed in 2021 if the trade deal between the two economies could not be made successfully. Moreover, the scenario modeling is used by the ADB Multiregional Input-Output Table (ADB MRIOT) for the year 2017 in order to quantify the impact of changes in tariffs working through local and production chains that provides advantages in individual economies and sectors as well as understanding the structure and evolution of global value chains. The direct impact of the trade conflict

is quantified at product level gathered by published lists of tariff affected commodities for all countries involved in the trade conflicts as of Sep. 2018. Additionally, these commodities are matched with detailed trade data from BACI and the United States Census Bureau in 2017 that uses a 6- to 10-digit Harmonized System classification [Abiad et al., 2018; Wang et al., 2018].

*Table 2.* Description and Size of Three Modeled Scenarios Between the U.S. and China

Scenarios	US Tariff Actions and Size of Impact	Retaliatory Measures by China	Date of Implementation
Current Scenario (measures implemented as of Oct. 2018)	30% and 20% blanket tariffs on all imports of solar panels and wash machines worth \$ 10.3 billion (0.4% of US imports)	China imposed 15% and 25% tariffs on \$3 billion worth of US goods (2.3% of US exports to China)	First quarter 2018
	25% on \$34 billion worth of Chinese goods (7% of Chinese exports to the US)	25% on \$34 billion worth of US goods (26% of US exports to China)	6 July 2018
	25% on \$16 billion worth of Chinese goods (3% of Chinese exports to the US)	25% on \$16 billion worth of US goods (12.3% of US exports to China)	23 Aug. 2018
	10% on \$200 billion worth of Chinese goods raised to 25% in 2019 (40% of Chinese exports to the US)	5%, 10%, 20% and 25% on \$60 billion worth of US goods (46% of US exports to China)	Begins 24 Sep. 2018 and escalates 1 June 2019
Bilateral Escalation Scenario (add 25% tariffs on all bilateral US China imports)	US blanket tariffs of 25% on 100% of Chinese exports to the US worth \$505.5 billion (an additional \$267 billion from previous scenario)	Chinese blanket tariffs of 25% on 100% of US exports to China worth \$ 130 billion (an additional \$17 billion added from previous scenario) Chinese blanket tariffs of 25% on 100% of US exports to China worth \$ 130 billion (an additional \$17 billion added from previous scenario)	Model assumed first quarter 2019, but delayed after second quarter
Worst Case Scenario (add 25% tariff on all autos, parts and retaliation)	US blanket tariffs of 25% on all imports of autos worth \$350 billion (14.5% of US imports equivalent to 0.44% of global GDP)	Retaliatory measures by other countries including China on all their auto and auto parts imports from the US worth \$130 billion (6.8% of total US merchandise exports)	Model assumed first quarter 2019, but delays third quarter 2019

*Source:* Author's own adaptation based on [Abiad et al., 2018].

Given the ADB analysis, the trade conflict between the two economies will be affected negatively in all scenarios. Under the current scenario, the Chinese economy would grow lower GDP by 0.48 percent, while the bilateral escalation scenario subtracts 0.55 percent GDP. In the worst case scenario, the Chinese economic growth could be less by 1.05 percent. By contrary, the U.S. economy could be affected by the trade conflict less than the Chinese economy. It could subtract 0.12 percent, 0.08 percent, and 0.24 percent respectively. It indicates that the trade conflict can impact on the two major economies rather marginal than expected in the midterm period although its impacts on Chinese economy are much higher than on the U.S. economy (see fig. 3, 4).

Another report analyzed by the Netherlands' government research institute represents the EU's perspective on the trade conflict between the U.S. and China. Given the longer term analysis of the baseline in 2030 on the trade conflict scenarios from World Scan simulations as the CPB's global CGE model, the macroeconomic results look similar. The baseline is in 2018

when business is as usual scenarios with no trade policy change and a trade shock with negative GDP effects due to the tariff increase start in 2019. The four scenarios are unilateral steel and aluminum tariffs by the U.S., scenario 1 plus retaliatory tariffs by China, the EU, Canada, and Mexico, scenario 2 plus US-China trade conflict, and scenario 3 plus 25 percent US tariff increase on automobiles and parts imports from the EU. In these scenarios, the impact of the trade conflict on the two major economies results also in marginal, and the U.S. economy is less vulnerable than the Chinese economy. The scenario 4 subtracts the former with  $-0.3$  percent and the latter with  $-1.3$  percent (Bollen, Rojas-Romagosa, 2018, table 3).

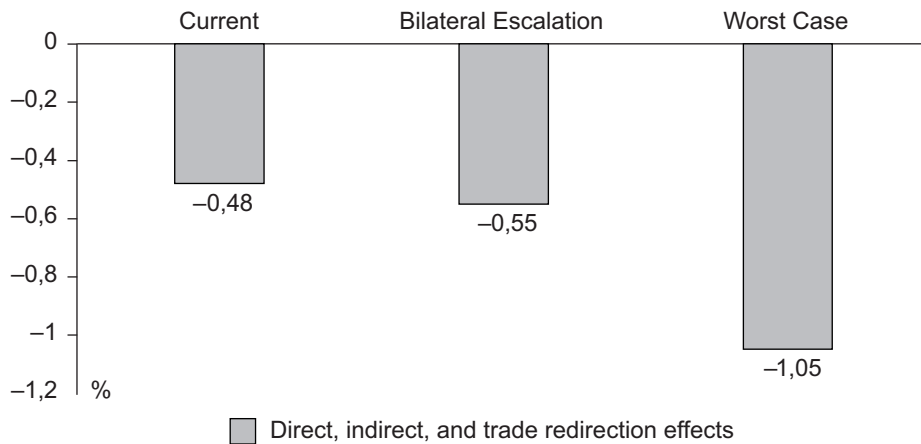


Fig. 3. Impact of the Trade Conflict on Chinese GDP by Scenarios

Source: [Abiad et al., 2018].

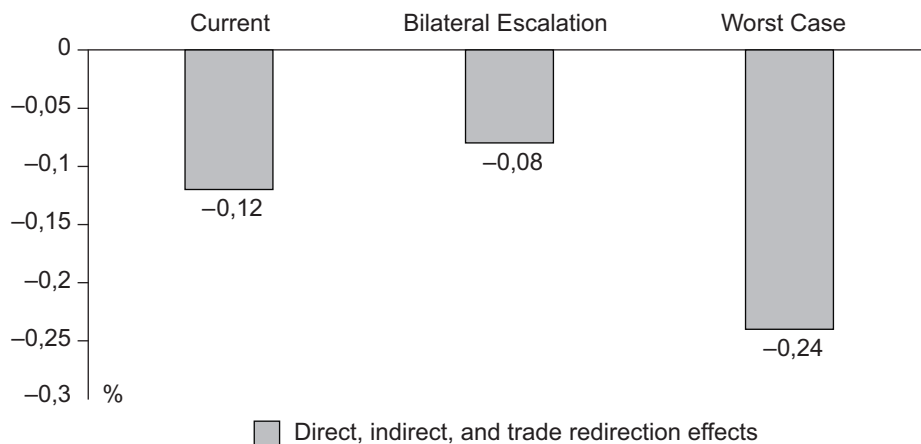


Fig. 4. Impact of the Trade Conflict on the U.S. GDP by Scenarios

Source: [Abiad et al., 2018].

Besides these four scenarios, there is scenario for trade conflict escalation between the U.S. and all OECD member nations including trade conflict escalation between the U.S. and China. In the scenario, the impact of the trade conflict on the two major economies could be

rather strong. It could subtract the U.S. economic growth with slightly over three percent, while the Chinese economy could generate over four percent economic growth loss [Bollen, Rojas-Romagosa, 2018].

*Table 3. Macroeconomic Effects of the U.S. and China Compared to the Baseline in 2030*

Scenarios	The U.S.	China
Scenario 1		
GDP (%)	0.0	0.0
Export volume (%)	−1.6	0.0
Import volume (%)	−1.0	0.0
Scenario 2		
GDP (%)	−0.4	0.2
Export volume (%)	−6.3	−0.9
Import volume (%)	−4.8	−0.9
Scenario 3		
GDP (%)	−0.3	−1.2
Export volume (%)	−13.5	−8.2
Import volume (%)	−10.5	−8.4
Scenario 4		
GDP (%)	−0.3	−1.3
Export volume (%)	−14.0	−8.3
Import volume (%)	−10.9	−8.4

*Source:* [Bollen, Rojas-Romagosa, 2018] based on World Scan simulations.

### ***Impacts on the World Economy***

Given the ADB analysis, the trade conflict between the two economies will be affected negatively in all scenarios even in the world economy although it will affect to the world economy less than to the U.S. and Chinese economies. Under the current scenario, the global economy would grow lower GDP by 0.08 percent, while the bilateral escalation scenario subtracts 0.07 percent GDP. In the worst case scenario, the world economic growth could be less by 0.25 percent. It shows that the trade conflict between the two largest economies will impact on the global economy nearly zero in the two scenarios, but affect very low in the worst case scenario in the midterm period. In the World Scan simulation, the impact of the trade conflict on the world economy could be from −0.1 percent negative economic growth to 0.1 percent economic growth in all scenarios [Abiad et al., 2018; Bollen, Rojas-Romagosa, 2018, fig. 5, 6].

Although the world economic growth ranges from −0.1 percent to 0.1 percent based on the World Scan simulation, some part of the world could be affected more negatively than other part of the world. East Asian countries supplying intermediate goods to China and exporting final products to the U.S. and the EU could be affected mostly negative. These nations are Korea, Japan, Singapore and Taiwan. Additionally, Australia, Indonesia, Thailand, and the Philippines exporting raw materials and industrial parts to China will be impacted negatively [Bollen, Rojas-Romagosa, 2018; IMF, 2019].

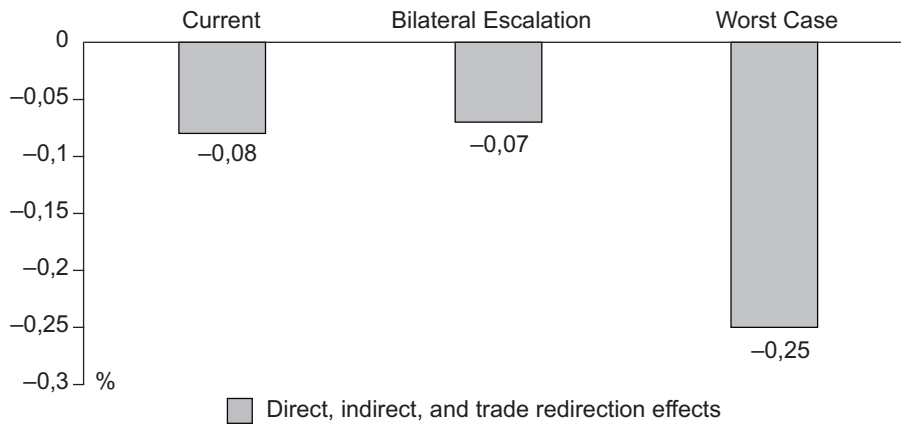


Fig. 5. Impact of the Trade Conflict on the World GDP by Scenarios

Source: [Abiad et al., 2018].

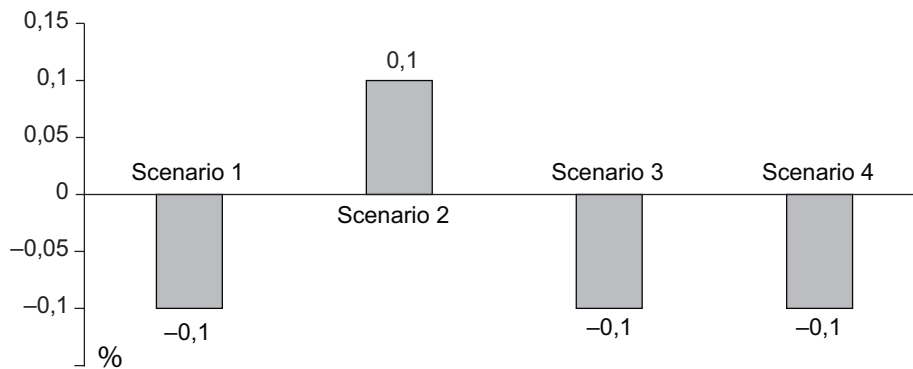


Fig. 6. Macroeconomic Effects of the World Economy Compared to the Baseline in 2030

Source: [Bollen, Rojas-Romagosa, 2018] based on World Scan simulations.

## Conclusion

Trade conflict has always existed in the global economy that is rather common because some trading partners gain more benefit than others. In the economic history, our lesson is that there is no winner from the trade conflict if it is not solved by dialogue and trade agreements. We have already experienced the Great Depression in 1929/1930 that resulted in the Second World War and the total destruction of the world economy. Unfortunately, we are again experiencing severe trade conflicts between the two largest economies in the 21<sup>st</sup> century that may impact on the global economy negatively if it continues without any proper solution.

First of all, ironically the trade conflict started from the U.S. pursuing trade protectionism particularly in the Trump Administration having various internal problems such as trade imbalance with its trading partners, income inequality, a vast government budget deficit etc. The U.S. government imposed high tariffs on imports of solar panel and washing machine first and later steel and aluminum from imports of its trading partners. After revising KORUS FTA and NAFTA, the U.S. government focuses on the trade dispute with China that is still ongoing

process threatening to impose 25 percent tariff on all import goods from China and vice versa. Furthermore, the U.S. government plans to impose 25 percent tariff on the import of automobiles and parts from all countries although it is delayed six months long from May 2019. Fortunately, the two nations agreed the trade deal and signed on it in Jan 2020 in order to solve the trade conflict. However, it is not fully clear that the trade deal could be implemented as planned because the two parties' interests are not fully matched.

Since the severe trade conflict between the U.S. and China started in early 2018, several global and regional institutes such as IMF, ADB, European Central Bank (ECB) started to analyze the impacts of the trade conflict between the two major economies as well as the global economy. Additionally, individual nations' economic think tanks also joined this trend. For the impact of the trade conflict between G2 on their national economies and the global economy in the midterm period, the analysis of ADB predicted a minor economic impact on the U.S. and China in the three scenarios although impact on China could be higher than that of the U.S. Additionally, the impact of the world economy in these scenarios could be very low. It may be the reason why the two major economies are not afraid of continuing the trade conflict because the trade conflict in all scenarios could impact on their economies marginal. Based on this reason, the trade conflict between the U.S. and China may continue at least in the midterm period if the both parties are not satisfied with the final outcome of their trade negotiation.

In the longer term perspective based on the World Scan simulations, the trade conflict between the two major economies could also generate marginal impacts on the U.S. and Chinese economies, while it would affect the global economy negatively except the scenario 2. However, the worst case is that the U.S. escalates trade conflict with all OECD member nations including the U.S. and China trade conflict escalation resulting in the impacts of high GDP loss on the U.S. and China with over three percent, and four percent respectively. Therefore, it is extremely important not only for the two major economies, but also for global economy to hinder the trade conflict from escalating and spreading out at the global level.

In fact, the trade conflict between G2 generates other issues such as technological dispute, financial conflict focusing on currency manipulation etc. In terms of the technological conflict, G2 competes with each other particularly in the 5G area that plays the core role in completing the Fourth Industrial Revolution. At present, China is ahead the U.S. in the area so that the U.S. government has tackled on suspending Chinese Huawei in the U.S. market due to the national security reason and asked its allies to follow the U.S. policy line. It means that the trade conflict is only a starting point for the technological supremacy and hegemonies power in the world politics and economy. Accordingly, it will spread out to other areas such as technology and finance continuously in the future.

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# Trade Policy and National Economic Interests in Korea

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## Abstract

*Membership in the World Trade Organization (WTO) and participation in free trade agreements (FTAs) are important instruments for governments to realize national economic interests. The Republic of Korea has been particularly successful in doing so. As the experience of Korea shows, a trade policy mix between multilateral liberalization under the WTO and preferential liberalization through FTAs allows the government to optimally balance national interests and strive for higher levels of social welfare and economic effectiveness, while simultaneously protecting national industries. However, such results seem to be possible only if national economic interests are clearly defined and are synchronized with a country's goals regarding WTO membership and its strategy for FTAs. During recent decades, Korea has practiced an active long-term planning of trade policy so that trade benefits are not excessively concentrated in a narrow range of trade actors and are distributed more evenly in society. This meant appropriate balancing of liberalization and protection measures, reinforced by special support programmes that neutralized the negative impact of higher market openness. In this article, Korea's strategy regarding trade policy is analyzed, including the reasons Korea pursued an FTA-centric policy and the benefits it obtained in addition to those it obtained from WTO membership.*

**Key words:** trade policy national economic interests; World Trade Organization; free trade agreements; Korea

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## Introduction

Trade policy is an important tool that can be used to stimulate growth of a country's national welfare. The role of trade policy is determined by its close links with spheres of trade, production, investment, and technological exchange, as well as by its fundamental role in promoting and protecting the interests of national manufacturers. Korea belongs to a group of states that achieved remarkable economic success due to an active use of trade policy that led to improvements in each of the areas mentioned above and beyond. Before the Uruguay round of multilateral negotiations began, Korea had been passively involved in discussion on liberalization

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of trade under the General Agreement on Tariffs and Trade (GATT), the predecessor of the World Trade Organization (WTO). However, when the round began in 1989 it became obvious that the multilateral trading system could offer the export-oriented Korean economy numerous benefits by bringing down barriers to international trade. The realization of new possibilities turned Korea from a passive developing country into a proponent and active user of trade policy as a tool to increase national welfare. Growth opportunities that the WTO opened for the country were in later years multiplied through free trade agreements (FTAs) that Korea had pursued since the end of 1990s.

This research analyzes the evolution of Korea's trade policy in 1990–2010s by focusing on the country's transition from a WTO-centric trade policy to an FTA-centric policy, identifies key elements of its FTA strategy, and investigates the effects of trade policy. Certain tactical manoeuvres that Korea used in order to protect and at the same time to promote its economic interests within the WTO are highlighted, as well as how the country changed from being a passive observer of negotiations on trade into an experienced negotiator capable of initiating agendas with its FTA partners. The research indicates that Korea's success was founded on a deep understanding of the nation's fundamental economic interests and the necessity of aligning trade policy with them. In Korea's case, economic rather than geopolitical or strategic interests have always been a priority in its trade policy. The Korean government has sought to go beyond an incremental increase in macro indicators, or creating benefits for certain groups of manufactures, to achieve higher economic efficiency of the national economic system. Business interests were considered based on their role in the national economy and their ability to contribute to economic growth.

The article offers conclusions regarding the key elements that have made Korea's trade policy successful which can be borrowed by other countries, including Russia.

## Korea's Economic Interests and Their Place in Trade Policy

Numerous studies analyze relationship between trade policy and welfare. One of the first works on the problem, entitled "Trade and Welfare," was published by Nobel Prize-winner J.E. Meade in 1950s [1955]; this work laid the foundations for other significant research on the issue. Some of the more widely known works include the contributions of M. Amiti et al. [2017], R. Baldwin [1989], M.L. Busch and E. D. Mansfield [2011], W.M. Corden [1997], J. Eaton and G.M. Grossman [1986], K. Handley and N. Limão [2017], P.R. Krugman and Obstfeld [2009], and U B. Marchand [2017]. Although this list is far from exhaustive it supports the idea of the potential of trade policy to influence national welfare. This influence is even more obvious in case of small, open economies, a group of countries to which Korea belongs.

Korea is highly dependent on international markets. Its exports and imports combined exceed 80% of the country's gross domestic product (GDP), pointing to the strong influence of the external sector on the domestic economy and, consequently, on trade policy. Historically, Korea was successful in its economic achievements because it relied on an export-oriented growth model [World Bank, 1993, pp. 127–130]. This link between growth and export performance shaped national economic interests.<sup>2</sup> Over years these interests were carefully calibrated and adapted in order to reflect changes in international and domestic economies, and policies to achieve them were re-aligned with new realities. At the early stages of development when the foundations of Korea's manufacturing industry were created, trade policy was subordinated to industrial policy, prioritizing the protection of national manufacturers from competing imports and rewarding aggressive export manufacturers [Amsden, 1992, pp. 139–55]. As a result, trade-

<sup>2</sup> For more on Korea's economic nationalism see [Lee, Lee, 2015].

related measures were increasingly protectionist. But in later years the situation had changed, prompted by the demand for a more liberalized and open foreign trade which has emerged from within the country.

As Korea's economy became more complex, it accumulated competitive advantage and integrated into global production and distribution networks, which lead Korea's policymakers to turn their attention toward achieving a higher degree of openness. Representatives of strong manufacturing industries like electronics, auto- and chemical industries, too, supported liberalization as they viewed it from the perspective of more growth through international expansion [Gills, p. 667]. However other industries were still too weak to be subject to international competition. So, Korea needed a solution that would balance limited liberalization with protection. Under those circumstances, liberalization under the rules of the international trading system was seen as an optimal choice because it was possible to combine reasonable openness with protection of sensitive industries [Kim, 2004]. In addition, as a member of the WTO, created in 1995, Korea had access to a dispute settlement mechanism that allowed it to resolve trade conflicts and prevent unfair trade practices applied by other member-economies.

Attitudes toward liberalization underwent a greater change at the end of 1990s as Korea entered a phase of economic reform. At the end of 1990s the industrial dirigisme of previous decades no longer served the needs of Korea's more advanced economy; the country needed more flexibility and openness to continue to grow. As a result, an FTA strategy was formulated and occupied a central place in the transition. It is reasonable to question why, at that time, Korea diverted its attention away from the WTO, which it had praised for creating new development opportunities just a few years before. This can be explained by two major factors: a failure to achieve swift progress on Doha Development Agenda (DDA), and the greater emphasis placed on regional integration by the U.S. and EU. Progress on the DDA was essential for the Korean government to realize its ambitions to grow into an advanced economy, but as the process stalled Korea switched to preferential agreements that could unlock capacity for the further increase of Korea's export's and, thus, sustain dynamic growth of the national economy [Sohn, Yoon, 2001, pp. 11–5]. In addition, preferential agreements, represented largely by FTAs, allowed Korea to proceed with its economic reform plan, triggered by the Asian financial crisis of 1997–98, to increase flexibility and efficiency of the system and domestic economic institutions, and to strengthen intra- and extra-regional cooperation [Ibid.].

The Korean government aligned WTO- and FTA-related issues with the country's long-term development goals focused on creating an advanced economy. Ministries engaged in continuous work to simplify regulation and harmonize evolving trade rules and measures with ongoing structural changes in the economy. For example, as the country's manufacturing sector embarked on a globalization strategy and strengthened its international positions in the 1990s, governmental support was reconfigured toward the service sector in the 2000s in order to lead this sector to successful internationalization. Such timely adjustments of priorities have helped to maximize benefits on the national level: when trade policy was used to solve problems of certain industries, it used a complex, multifaceted approach that took into account interests of all parties – the state, business and society. If entry barriers for manufactured goods were removed, companies became eligible for indirect support of their activities, in the form of easier access to finance or additional government orders, which neutralized potential negative effect from liberalization.

Let us consider how some of the major indicators characterizing Korea's level of welfare have changed during the period of active trade policy from 1990–2018. According to statistics prepared by the United Nations Conference on Trade and Development (UNCTAD) and presented in Fig. 1, during this period the country's GDP increased fourfold from \$360 billion to more than \$1,600 billion. Another very important welfare indicator – GDP per capita – grew

at a similar magnitude from \$6,500 in 1990 to \$31,700 in 2018. Growth of these indicators in Korea looks even more remarkable if the fact that the country had to recover after two serious downturns is taken into account. One of the downturns followed the Asian financial crisis of 1997–98 and the second one was caused by the financial crisis of 2008. Despite these, Korea managed to make the transition from the group of higher middle-income countries to the high-income cohort.<sup>3</sup> Also, in 1996 Korea joined the Organisation for Economic Co-operation and Development (OECD) – an organization with members from developed economies only – an event that recognized Korea’s economic achievements (although by the World Bank’s classification it still formally belongs to a group of developing countries).

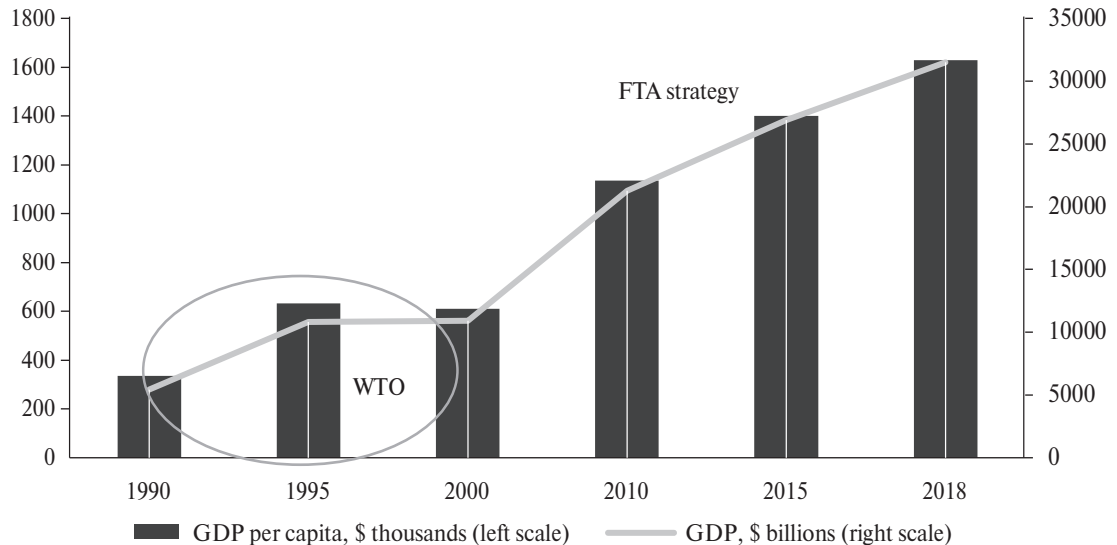


Fig. 1. Korea’s GDP and GDP per Capita in 1990–2018 and Phases of Its Trade Policy

Source: [UNCTAD, n. d.].

Trade growth, both in absolute indicators and as a share of world trade, was another achievement that Korea realized in the course of its active trade policy. For example, during 1990–2018, overall exports increased 9.3 times more dynamically than imports (which grew 7.7 times) despite starting from approximately the same level (Fig. 2). Trade liberalization through FTAs has contributed to this growth. Moreover, due to favourable terms of trade (higher exports and lower imports) Korea accumulated a significant trade surplus: in 2018 it was equal to \$69.6 billion, or almost 10% of Korea’s total exports. The existence of a surplus was a major change from previous decades during which Korea had struggled to keep its imports at lower levels than exports. Export growth had a positive impact on Korea’s share of the world trade, which grew from 1.8% in 1990 to 3.1% in 2018.

Adaptation of national trade policy to WTO, and later FTA, requirements has transformed Korea’s role in the international division of labour. In the 1990s Korea was predominantly a supplier of finished goods, but liberalized and simpler trade procedures have facilitated its transition to a supplier of intermediate products. In a study done by the WTO and the Japan External Trade Organization (JETRO) in 2011, it was emphasized that the country had improved its position as a supplier of high-tech intermediate products within Asian value chains

<sup>3</sup> In 1990, high income level was \$7,620; by 2018 it had risen to \$12,376 [World Bank, n. d.].

[IDE – JETRO, WTO, 2011, pp. 85–6]. Consequently, this change was reflected in the product structure of Korean exports. As of 2018, the share of intermediate goods in Korea's industrial exports was 36% [World Bank, n. d.]. Specificities of trade in intermediate goods prompted the development of related services in Korea, stimulating further growth of the service economy. Korean logistic, insurance, and financial sectors became much stronger players as a result of their new role within regional and global value chains.

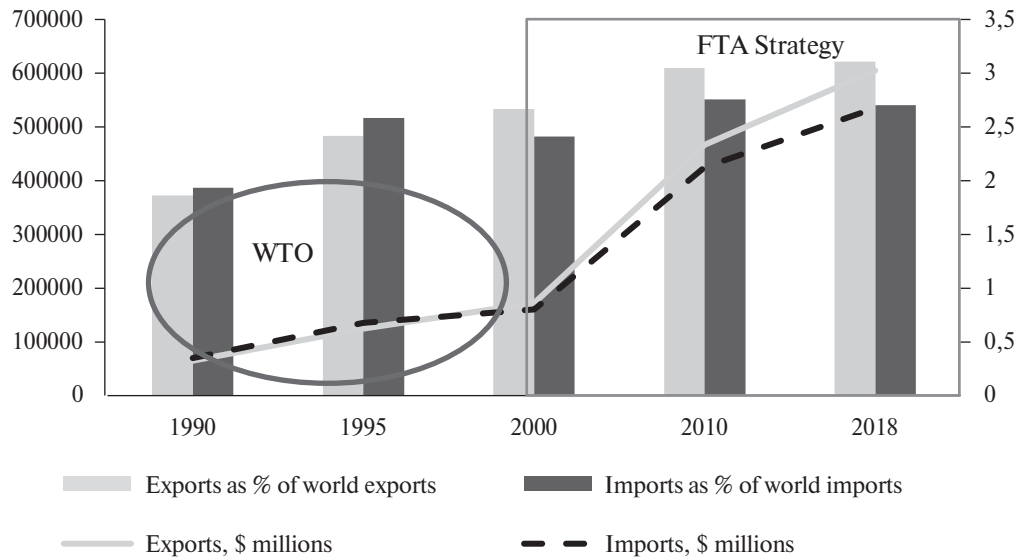


Fig. 2. Korea's Foreign Trade, 1990–2018

Source: [UNCTAD, n. d.].

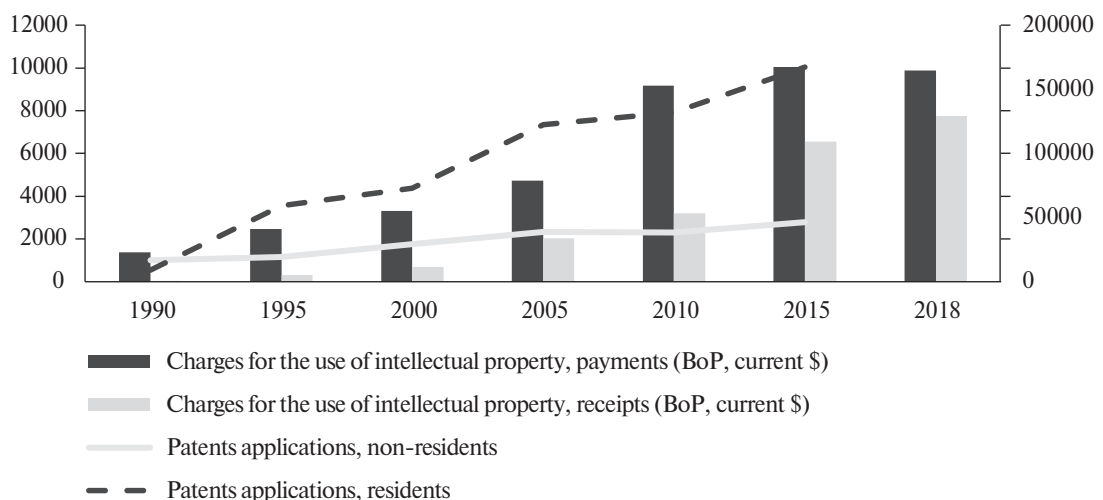


Fig. 3. Number of Patent Applications and Proceeds for the Use of Intellectual Property Rights and Korea's Balance in Technological Trade

Source: [World Bank, n. d.].

Another important change that reflects how much Korea has gained in welfare occurred in the technological sphere. Korea has become a leader among OECD countries in research and development (R&D) spending relative to GDP, raising its gross financing of R&D from 2% of GDP in 1990 to 4.2% in 2018. More importantly, this spending generated results in the form of actual increases in patenting activity. In 1990 non-residents had outperformed residents in the number of applications for patents (Fig. 3), while in 2018 the situation reversed as residents applied for 167,000 patents versus 46,000 filed by non-residents [OECD, 2019]. As a result of this growth, Korea started to receive income from the transfer of intellectual property rights (as reflected in Fig. 3). Of course, this did not change Korea's status as a net-importer of technology, but it is a positive, stable trend toward greater exports of innovation products.

## The WTO and Korea's Economic Interests

The international trading system, formerly GATT, played a central role in Korea's economic achievements [Hyun, 2003]. Being part of the system from the early years meant that Korean trade policy has had an opportunity to observe changes in global approaches toward trade policymaking and develop in tandem with them. GATT rules regarding most-favoured-nation (MFN) and a clause about market access for the least-developed countries gave Korea opportunities to pursue a limited trade openness for imported inputs and at the same time practice industrial protectionism. The least-developed country clause unlocked access to developed markets and made Korea eligible for low levels of import tariffs when exporting to advanced countries while maintaining high import tariffs for industrial goods at home. The "infant industry" argument, very common among developing countries in the 1970–80s, also helped to justify protectionism [Korgun, Popova, 2011].

After the WTO was created, Korea continued to receive the benefits associated with its developing-country status despite the success of its development programme. This status enabled more flexible schedules for tariff reduction and longer adjustment periods for sensitive industries. In Korea's case, agriculture, the service sector and the sphere of intellectual property rights benefited from arrangements that allowed longer timelines for bringing national regulations into compliance with WTO norms. The Korean government used this time wisely and introduced measures to support weak sectors (mostly R&D financing) and to prepare them for future liberalization.

As a result of the Uruguay round, Korea accepted a level of liberalization for its industrial sector on the same scale as developed countries; in effect, this meant that Korea was ready to abandon distortional policies for industrial protection, such as high tariffs, preferential financing, and the subsidizing of domestic manufacturers. Table 1 provides a snapshot of how Korea has kept its commitments for industrial market access and tariff binding in the WTO. As the numbers show, progress was substantial: the average applied rate decreased from 20% to 9.8% for industrial goods and from 72.4% to 58% for agricultural products in 1996–2018. In addition, Korea joined some countries in initiating an agreement on 0%-level tariffs for trade in electronic goods and information technologies.

Assessments conducted by the Korean government found that during the first several years following the creation of the WTO, Korea gained \$28 billion as a result of lower barriers to exports negotiated during the Uruguay round [Republic of Korea, 1996, p. 20]. In 1995 Korean exports were worth \$125 billion and multilateral liberalization of trade added approximately 20% to that, stimulating domestic industrial production. More flexible terms of liberalization in other sectors mentioned above, were, also considered a success and in line with national economic interests.

*Table 1. Changes in Korea's Tariff Rates After the WTO Was Created, 1996 and 2018*

	<b>1996</b>		<b>2018</b>	
Binding Coverage, %	91.0		94.9	
Tariffs	Simple Average	Simple Average MFN Applied	Simple Average	Simple Average MFN Applied
All tariff lines	27.6	14.4	16.5	13.7
– agricultural products	72.4	51.8	58.0	57.0
– non-agricultural products	20.0	7.7	9.8	6.7

*Source:* [Republic of Korea, 2004, p. 43–44; WTO – ITC – UNCTAD, 2019, p. 111].

Thus, despite having formal status as a developing country, until October 2019 Korea practiced a dual status inside the WTO, trying to realize gains meant both for developed and developing countries. This dual status markedly differentiated Korea from other member-economies that belonged either to developing or developed groups of countries. This dual status laid the groundwork for a sophisticated manoeuvring of trade policy by Korea which is still viable in today's FTA-centric trade policy.

Fundamentally, the Uruguay round was the first round of negotiations in which Korea openly faced pressure from developed countries had to be active in protecting its interests. Successful results and apparent benefits for the national economy transformed how Korea approached the formulation of its trade policy, and actually brought trade policy to the forefront of instruments used to increase national welfare. From that point on, Korean trade policy became very active, and at times even aggressive, when thinking about the multitrack FTA strategy it had pursued since late 1990s. The normative aspect of the WTO's rules for trade regulation was borrowed and implemented in Korea's FTA strategy. Issues regulated by the WTO formed the basis for texts of FTAs and lack of progress in further WTO negotiations made Korea broaden scope of its FTAs.

Finally, China's accession to the WTO in 2001 had a positive impact on the Korean economy. At a time when Korean economy was struggling with sluggish domestic demand after the domestic credit card bubble of 2003, Chinese was able to support Korean manufacturing and GDP growth. The correlation coefficient between rates of GDP growth and growth rates of Korean exports to China in the 2000s (Fig. 4) is very strong, suggesting the existence of dependency. For 2003–13 the correlation ties are even stronger, reflecting the growing dependence of Korea's economic performance on external trade to enhance the value of the trade policy overall.

Due to China's commitment to decrease barriers to trade, Korean companies, both large and small- and medium-sized business, received opportunities to enter one of the world's biggest markets. The geographical proximity of the two countries was an additional advantage. As a result, in 2004 China became the largest trade partner of Korea, making up 30% of Korea's total foreign trade [KITA, 2019]. Also, China became the largest recipient of Korea's outward foreign direct investment (OFDI) as in 2003–05 40% of Korea's total OFDI went to China's manufacturing industries [The Export-Import Bank of Korea, n. d].

Korean FDI in China contributed to the development of regional and global value chains. While Korean firms supplied intermediate inputs, they were also filling up demand for domestic manufacturing industry. Until 2013 over 35% of parts and components exported from Korea went to China. In addition, since 2005 intermediate products have made up more than 60% of Korea's total exports to China [KITA, n. d.]. High-tech industries were strongly involved

in this trade exchange from Korea's side; in particular electronic, electric machinery, and auto industries have benefited the most since they provided more than half of the country's intermediate exports [Ibid.]. According to research by the Korean Institute of International Economic Policy, the formation of such manufacturing and distribution networks improved competitiveness and effectiveness of Korean business in the international arena.

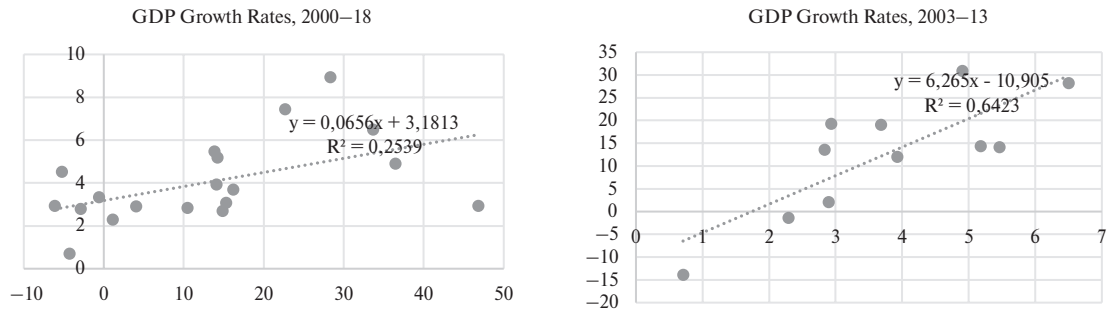


Fig. 4. Results of Correlation Analysis Between Rates of Korea's GDP Growth and Growth Rates of Export to China in 2000–18 and 2003–13

Source: Calculated by the authors.

Overall, the GATT and WTO multilateral trading system presented Korea with real opportunities to realize the potential of its export-oriented industry, increase the scale of its economy, and adapt its domestic regulation system to international practices. Korean companies employed opportunities created by reduced barriers to trade as they were able to increase export production and improve their international standing despite slower domestic demand. While the export sector was growing, the Korean government took measures to protect and support sensitive sectors, providing tools to prepare them for future liberalization.

## Free Trade Agreements and Korea's Economic Interests

At the end of 1990s Korea started to appreciate the necessity of FTAs for continued development. Initially, this realization was a reaction to the spread of integration initiatives in the world, but in later years it grew into a strong belief that FTAs were necessary in order to transform the Korean economy for the future [Sohn, Yoon, 2001, p. 15]. In the second half of the 1990s the national leadership expressed deep concerns that its major trade partners – the U.S. and European countries – were preoccupied with their own regional integration projects. It was feared that regional integration would create obstacles for Korea's export-dependent economy and distance it from its main export markets and sources of investments [Ibid., p. 14]. Asian neighbours, too, provided enough reasons for similar worries. Japan and China showed interest in the Association of Southeast Asian Nations (ASEAN) and embarked on strategies for regional integration, whereas Korea remained passive. Korean political circles were slow to accept preferential agreements because they meant a departure from multilateralism which, while still rather new, was more understandable to them. Moreover, they did not want additional liberalization beyond the scope of Korea's WTO commitments. As a result of such sentiments, in 2003, among the WTO members only Korea and Mongolia did not have a single FTA [Liou, 2008].

However, lack of progress on the DDA gave Korea a strong incentive to launch an FTA strategy. After the failure of the ministerial meeting in Seattle in 1999 it became obvious that the

country needed alternatives to multilateralism to expand its trade and sustain economic growth [Park, Moon, 2006]. President Roh Moo-hyun referred to FTAs as an existential choice for his country, whose welfare depended on openness to trade [Liou, 2008, p. 186]. Providing further arguments in favour of an active FTA policy, the Korean government paid attention to such benefits as better, deeper and more effective economic cooperation with individual partners and, more importantly, new opportunities to compete with Japanese and Chinese manufacturers in third countries due to the fact that FTAs would improve the price positioning of Korean products through lower tariffs.

The choice in favour of FTAs has not been easy for Korea and involved political debates inside the country. Some representatives of political elites were against further liberalization because they saw it as a threat to agriculture, in the first place, and other weaker industries [Ibid., p. 184]. The FTA with Chile, the first FTA for Korea initiated in 1999, became a victim of these debates as its ratification was delayed by three years because the Korean parliament could not come to consensus on the necessity of the FTA strategy. A breakthrough came only when Korean companies started to lose market share in Chile to Japanese and Chinese competitors. In the end, the Korea-Chile FTA was ratified in 2004 and gave a start to Korea's active, sometimes even aggressive, strategy in matters of regional integration.

Korea's FTA strategy was based on three pillars corresponding to the its national goals. The first and most important one was to secure agreements with the U.S., the EU and China, as these markets could provide demand for Korean products, grow trade in services and improve access to technologies [Sohn, Yoon, 2001, p. 10]. The next priority was to initiate FTAs with Asian partners – to deepen cooperation with ASEAN and create conditions for a trilateral FTA between Korea, Japan and China.<sup>4</sup> Finally, Korea planned to make extra-regional agreements in order to expand market horizons beyond traditional spheres of interest and to increase the globalization of the Korean economy. The FTA with Chile fell under the last pillar as it opened a window for Korea into Latin American markets where it was under-represented at the beginning of 2000s.

Realization of this strategy and particularly its third part implied that smaller countries with more or less complimentary interests would initially be chosen as FTA partners in order to avoid difficulties during negotiations [Koo, 2008; 2010]. After Chile, Singapore and the European Free Trade Association (EFTA) became Korea's next partners. They were economies with small agricultural sectors located in different geographical areas close to big markets. The first three agreements gave Korea enough confidence to move closer to its main goal and open negotiations with the U.S., the EU and China at the end of 2000s. Many negotiations took place simultaneously as the Korean government wanted to maximize outcomes in the shortest amount of time. By the end of 2018, in 16 years Korea had managed to sign and ratify 16 FTAs (with Chile, Singapore, EFTA, ASEAN, India, the EU, Peru, the U.S., Turkey, Australia, New Zealand, Columbia, Canada, China, Vietnam and Central America); an additional three FTAs are signed and awaiting for ratification, and seven more are under negotiation (including an FTA with Russia). There are another three feasibility studies under way [Korea FTA, n. d.].

As mentioned above, in the first years of its FTA strategy Korea used the WTO agenda to negotiate FTAs. This resulted in many similarities among its first FTAs with a range of issues discussed under the WTO framework. Agreements with Chile, Singapore, EFTA and Vietnam primarily regulate national treatment and market access, rules of origin, customs procedures, safeguard measures, antidumping and dispute settlement; they hardly touch

<sup>4</sup> Despite multiple rounds of negotiations, the agreement between Korea, Japan and China has not been signed due to numerous disagreements on agricultural and non-agricultural market access, IP protection, and some ongoing historical disputes.

trade in services and do not venture into other issues [Koo, 2008]. For example, the Korea-Chile and Korea-Singapore FTAs practically copy Uruguay round questions as they revolve around barriers to trade and protection of sensitive sectors. In later agreements, though, Korea became more ambitious and included a wider range of issues, such as the environment and development, which do not directly relate to trade. Later agreements include measures to reduce barriers to trade in services, stricter application of intellectual property (IP) protection (starting from the KORUS FTA), protection of geographical names (KOREU FTA), migration (KORCHINA FTA), and environmental protection (FTAs with the U.S., the EU and China) [Korea FTA, n. d.].

However, despite numerous similarities with the WTO in approach to trade regulation, FTAs had their own value added. In case of the early agreements this came in the form of better terms of market access for Korean export-oriented companies because they could enjoy lower import tariff rates. In addition, the Korean government was able to exclude from the agreements sectors that needed protection due to national security concerns or simply because they were too weak to compete.

The extent to which Korea was able to intensify export growth through its early FTAs can be determined through a comparative analysis of export flows to the three markets – Chile, Singapore and EFTA – before and after FTA with each partner was ratified, using the methodology outlined in the manual of the Asia Development Bank [Plummer et al., 2010]. This methodology is based on calculating a weighted average of exports growth rates before the FTA came into force and then extrapolating these results onto the period after the FTA came into force. After extrapolation, the calculated and real value of exports were compared. A four-year period was used for analysis. Since the Korea-Chile FTA took effect in 2004, the analysis focused on the periods 2000–03 and 2004–07; FTAs with Singapore and EFTA came into force in 2006, so the periods analyzed were 2002–05 and 2006–09. Results of the analysis are summarized in Table 2.

*Table 2.* Calculated and Real Growth Rates of Korean Exports to Chile, Singapore and EFTA After the Ratification of FTAs

	Calculated Four Years After the FTA	Actual	Difference Between Actual and Calculated, %
Chile	587315.3	3115103	4.303971
Singapore	11800845	13616994	0.1539
EFTA	1456242	1956196	0.343318

*Source:* Authors' calculations.

If an FTA with Chile had not been signed, Korea's exports to this country would have been 430% lower than its actual value in 2007; thus, the effect of lower tariff barriers as a result of the FTA was considerable. In the cases of Korea-Singapore and Korea – EFTA FTAs, the magnitude of difference was smaller but still in the same direction as the real values of export in the fourth year after the FTAs came into effect were higher than the calculated values. More importantly, a positive effect was observed despite decreases in Korean exports to these markets in 2007 (exports to EFTA decreased by 35%) and 2009 (exports to Singapore decreased by 16% and to EFTA by 22%).

Overall, the FTA strategy had a positive effect on Korean exports to FTA-partner countries. According to estimates by the Korean Customs Office, the maximum effect was achieved

between three and four years after ratification of an FTA [Customs, 2019]. The rate of FTA utilization by Korean businesses is high too, and as of 2018 it achieved 70%. The FTA with Canada has the highest utilization rate (over 80%) and the same is true for the U.S., the EU and Chile, while the lowest utilization rate is of the FTA with China. Korean consumers also see the benefits of their country's FTA strategy. In 2019 in a survey of Korean consumers regarding their assessment of FTA policy, 67.5% of respondents had a positive opinion, which is 21% higher than in 2015 [Customs Office of Korea, n. d.]. Consumers observed the largest effect in the diversification of product choices and in decreased prices of imported goods and services [Korea Consumer Agency, n. d.].

In the case of later agreements, value added could be considered through the internationalization of Korea's service sector, more trade in products subject to IPR protection, and transformation of the Korean economy. However, it should be noted that although FTAs provided stimuli for expansion of trade in services, this issue was treated unequally in different FTAs. The most robust provisions for trade in services were set in the KORUS FTA while other deals have a more modest framework. In most cases agreements discuss transborder trade in services, but some FTAs only mention the issue without getting into much detail. The Park Geun-hye government considered the inclusion of trade in services within the KORChina FTA to be a diplomatic success because until then China had not discussed the issue in other FTAs. Let us consider major tendencies in service trade between Korea and the U.S., the EU and China to see whether and how patterns of trade in services changed.

The KOREU and KORUS FTAs, ratified in 2011 and 2012 respectively, had a positive effect on Korea's trade in services with these partners. The effect was also felt in the technological sphere, which is captured by statistics in proceeds for the use of intellectual property rights. By 2016 trade in services with the EU had grown by 15%, and with the U.S. by 6% compared to pre-FTA levels in 2010 (Fig. 5). In the case of the KORChina FTA, trade in services showed high growth rates in 2011–14 before the FTA was signed. Trade in services expanded due to active exports from Korea and much less from Korea's imports from China. But bilateral trade suffered from tensions between the two countries following deployment of the Terminal High Altitude Defense (THAAD) on the territory of Korea by the U.S., an action that was protested by China [Reuters, 2017]. Despite this temporary difficulty, the Chinese service market represents a high potential for Korea's export of services; moreover, it is a market where the balance of trade in services is to Korea's advantage. China presents opportunities for Korea to balance deficits in trade with other countries. Currently, the two countries are in the process of negotiating an additional agreement on trade in services.

Despite the negative balance in services trade with the EU and the U.S., its size remained stable after the FTAs were ratified. This means that Korea grasped opportunities to export services in parallel with growing imports of services from its partners. One of the most dynamic areas opened for Korea by FTAs is in commercial services.

In case of the KOREU FTA, a marked increase in proceeds from the transfer of intellectual property rights was also observed. Over the period 2011–16, Korean exports in this category grew from \$500 million to \$1.2 billion while imports from the EU reached \$2.7 billion in 2016. In the same year Korea transferred \$5.6 billion to the U.S. in the form of payments for intellectual property rights use (in 2011 Korea imported \$4.6 billion worth of services) while Korea's own exports to the U.S. were worth \$700 billion (\$1.6 billion in 2011) which is much lower than to the EU. The rapid increase of Korea's imports in the category under discussion was due to increasing transfer of technologies. Thus, after the signing of FTAs access to technologies for Korea had widened.

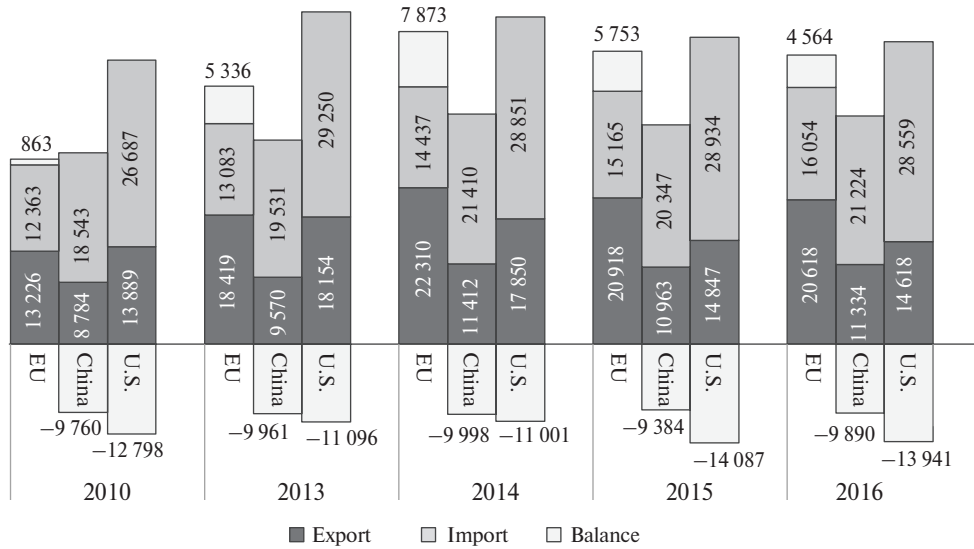


Fig. 5. Korea's Trade in Services With China, the EU and the U.S., in 2010–16, \$ millions

Source: Compiled by the Authors Using UNCTAD [n. d.] Statistics.

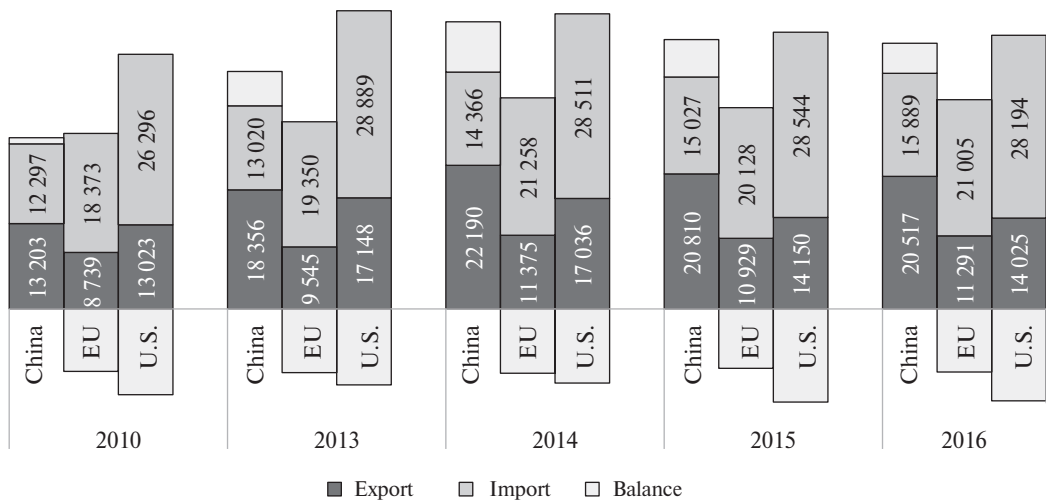


Fig. 6. Trade in Commercial Services Between Korea and China, the EU, and the U.S., 2011–16, \$ millions

Source: Compiled by the Authors Using UNCTAD [n. d.] Data.

Effects from the FTA policy were felt beyond the growth of trade. The overall level of openness of the Korean economy and the quality of the domestic business environment has improved markedly. The Korean government succeeded in reducing the amount of trade and business-related regulation through continuous revision and streamlining. As a result, Korea has moved up in international business ratings. For example, in 2005–06 the country occupied

27th position in the Doing Business rating published by the World Bank, but in 2020 it was in 5th place, ahead the U.S. and the UK [World Bank, 2020]. Korea has shown remarkable progress in decreasing the time and bureaucracy associated with launching a business. It is now among the leading countries in ease of trade procedures, observance of contractual obligations, convenience of the tax system, and protection of minority shareholders rights.

FTAs have produced some unforeseen effects as well. The process of negotiating FTAs has paved the way for different parties inside the country to work together to reconcile their interests in order to achieve benefits for the nation. The interests of manufacturers and agricultural producers had to be balanced through various mechanisms. One of the mechanisms the Korean government used involved special support measures to compensate losses associated with FTAs. Such measures were first introduced with regard to FTAs with the EU, the U.S., China, Vietnam, and New Zealand, and included export support through easier access to financing, additional investments to R&D to help to increase competitiveness of exports, and infrastructure funds for agriculture, among other things. Other mechanisms that proved to be quite effective were consultation services that explained how FTAs work and how businesses can take advantage of them. Relevant ministries ran special programmes for small- and medium-sized enterprises on a regular basis and created an online system to check the spectrum of tariff rates for each FTA. This mechanism proved to be so effective that a similar system was later done for the WTO so that companies can check WTO-related regulations. At the request of businesses, the Korean government created a committee to deal with the negative effects of FTAs. Any company can file a complaint and a committee has to investigate and reply to their request.

At the regional level the FTA strategy gave Korea more authority in trade negotiations. One of Korea's advantages that helped to maximize its number of FTAs was that Korea neither offered a competing integration programme nor exercised pressure to achieve a desired outcome or tried to suggest a normative base to unify regulation. Rather, it approached its partners in search of mutual economic benefits. At the start of its FTA strategy Korea did not suggest negotiating agendas and relied instead on existing WTO formulas. As it accumulated experience it began to take bolder actions and to include new issues on the agenda with support from its partners. Because it had experience, it could refer to already existing FTAs to provide a rational argument. Each new FTA served as a stepping block for the next one. In the end, the FTA strategy helped Korea to take its regional role more seriously and to show initiative on various regional matters.

Under the current situation one more positive aspect of the FTA strategy can be identified. As uncertainty remains about the future of the WTO appellate body that deals with disputes, FTAs allow Korea to regulate cooperation with its partners and manage disputes. FTAs serve as a safety valve that Korea can use in case of emergency in multilateral procedures.

## Conclusion

Korea's experience supports the idea that trade policy can be a powerful tool to achieve national goals including raising welfare. Its influence stretches beyond trade in goods to services and technology. In the case of Korea, trade policy also helped to balance the sometimes polarized interests of national producers and facilitate transformation of the economy. Korea started to use trade policy actively in the mid-1990s, and since then the country improved its global standing both in terms of GDP and business environment. Much of the success can be attributed to the role of the Korean government, which was able to find an optimal balance between the possibilities provided by a multilateral trading system and preferential trade agreements. Even when Korea has shifted toward FTAs, it continued to derive benefits from WTO membership including, those associated with China's accession.

Several aspects were key in enhancing the effectiveness of trade policy for the purpose of advancing national interests. In the first place, the Korean government determined its goals in each dimension (multilateral and preferential) of its trade policy. In case of the WTO, questions of protection for weak sectors of the economy and promotion of Korea's exports globally were prioritized. FTAs, in their turn, served to create additional advantages for entering new markets and promoting exports of other sectors – things that were hard to achieve through WTO membership.

Second, Korea's case shows that an FTA strategy can produce swift results because the country used a gradual multitrack model of negotiation moving from weaker to stronger partners and opening several negotiations simultaneously.

Third, gains from trade policy were distributed between economic agents at different levels, which enhanced the impact of the trade policy. The government initiated various training programmes for business that explained how to use FTAs or the WTO in their activities. As a result, rates of FTA use are relatively high.

Fourth, the agenda for FTA negotiations was broadened gradually. Korea created momentum as it coordinated different agreements and adjusted its regulations. The broadening of the issues was also beneficial because, as a result, Korea was able to suggest a clear economic programme and avoid sensitive political issues with its economic partners.

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