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# Transatlantic Strategy Group on the Future of US Global Leadership

## Session Three: Global Institutions and the Economy of the Future

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**G | M | F** The German Marshall Fund  
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STRENGTHENING TRANSATLANTIC COOPERATION

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On 10 June 2015, Chatham House and the German Marshall Fund of the United States, in partnership with the Bertelsmann Foundation, organized the third workshop of the **Transatlantic Strategy Group on the Future of US Global Leadership**. The event, entitled ‘Global Institutions and the Economy of the Future’, took place at the Bertelsmann Foundation offices in Berlin, Germany. It brought together 22 experts, scholars, officials, journalists and corporate representatives from Europe and the United States. The discussions were held under the Chatham House Rule. The following summary sets out the key points made but does not reflect any consensus among the attendees.

### Key points

- **The West is no longer able to drive the global economic order by itself.** The United States and Europe need allies in Asia and elsewhere to maintain economic stability. The global economic system is increasingly unfit for purpose – as evidenced by the rise of other structures such as the G20, the Asian Infrastructure Investment Bank (AIIB) and regional trade agreements – and it is not yet clear that a new structure is emerging to replace it. Current institutions need reform to allow rising powers (such as China and India) into the system.
- **The West needs to consider what changes it is willing to make to the current system to accommodate countries like China and India.** Many in the West believe that emerging powers need to be ‘integrated’ (language often seen as condescending by those very actors) into the current structures. But little thought has been given in the West to the compromises that could accommodate emerging countries – measures that could be more constructive than continuing to try to impose existing rules.
- **Despite the standard ‘rise of the BRICs’ narrative, there is huge divergence among rising economies.** China’s growth is slowing, Russia is in deep recession and Brazil is having severe economic problems. The common tendency of ‘straight-line’ thinking (believing that a current trend will continue unaltered indefinitely) is a mistake. For example, the convergence of China’s GDP per capita with that of the United States has slowed considerably in the past decade.
- **Proposed agreements such as the Transatlantic Trade and Investment Partnership (TTIP) and the Trans-Pacific Partnership (TPP) could have hugely significant strategic implications, but this dimension has not been a central part of the dialogue in Europe.** In Europe, the deals have largely been framed in economic terms, while domestic debates have often ignored the broader implications.
- **With the focus on overall growth rates, the lack of attention paid to inequality in Europe (and elsewhere) has the potential to cause significant economic and political repercussions.** Those parts of Europe that have been left behind economically have seen a dramatic rise in populism and nationalism. Yet policy-makers have been focused more on overall growth rates rather than on efforts to alleviate inequality.

### The future of global institutions

- **There is a slow move away from multilateralism towards bilateral and regional frameworks.** Nevertheless, existing institutions should not be discarded. Many work reasonably well, and it would be a mistake to disband them.
- **For global institutions to remain viable, emerging powers must have more influence in them.** Transatlantic powers acknowledge the need for reform, but they have not decided or found consensus on the specific changes to be made. If this process is resisted by existing powers, then alternative informal institutions, dialogues and groupings will develop in parallel. Current examples include the ‘BRIC’ (Brazil, Russia India, China) grouping, ‘IBSA’ (India, Brazil, South Africa) and the Shanghai Cooperation Organisation. Any emergence of parallel structures, however, is unlikely to be on terms favourable to the West.

- **Western countries should not underestimate the depth of anti-Western sentiment.** The legacy of colonial exploitation is not easily forgotten and is often reinforced by the international community's attempts to lead or shape policy in emerging countries. Events such as the US-led invasion of Iraq in 2003 and the global financial crisis in 2008–09 reinforced emerging powers' suspicion of international institutions and the West.
- **Despite the criticism it has faced, the World Trade Organization (WTO) will not disappear.** The WTO needs significant reform but there is no consensus for this. Rather, its role will change over time; it is already moving away from its convening role and towards an increasing focus on enforcing existing trade rules and settling disputes.
- **Regional agreements, such as TTIP and the TPP, may help to break the deadlock in multilateral trade negotiations.** Such agreements could be especially effective if they were designed to be open to future growth in membership.
- **The AIIB by itself is not particularly damaging for the West. In many ways it is a useful mechanism** for China to use excess capital and make vital improvements to regional infrastructure. However, it is a symptom of a broader trend: the West no longer writes the rules. Russia, too, is trying to create alternative global financial mechanisms and institutions to reduce the power of the West and limit the impact of sanctions.
- **Transatlantic powers have long experience in international institution-building, and in promoting the principles of conditionality on which they are based.** The experience acquired from the IMF and the European Union constitutes a decisive advantage in the competition between different models of international institution. China and Russia will need time and investment to learn how to manage alternative organizations.

### The impact of regional trade agreements

- **TTIP has been overhyped by both its proponents and its opponents.** In part this is due to poor framing of the debate by transatlantic political leaders and a lack of transparency in negotiations in Brussels. The deal is less about trade barriers and subsidies and much more about regulatory convergence. However, it is difficult to achieve the latter. TTIP is not going to produce new jobs or radically alter growth rates – however, it will lead to a better global division of labour. Its main benefits for society are likely to be higher productivity and efficiency. Advocates of TTIP should emphasize not that it will create jobs, but that it will improve the *quality* of jobs.
- **The strategic implications of TTIP and the TPP have not been explored in detail.** While there are economic benefits, trade deals clearly have an important strategic impact, bringing nations together and creating a common regulatory framework and level playing field. These deals can lead to the development of new global standards and, potentially, to new global architectures. They can also bring other players to the table, such as in the case of Japan engaging with the US following the US–South Korea deal and China looking for a European free-trade agreement after TTIP was announced.
- **The TPP and TTIP both face domestic hurdles.** The TPP is controversial in many parts of America and Asia, while TTIP is equally controversial in parts of Europe – particularly Germany. The apprehension in Germany partly originates from general anti-Americanism with roots in (among other issues) the Iraq war, the Snowden revelations, and a deep-seated fear of globalization and the power of large (particularly American) corporations.
- Trade deals have winners and losers. **Trade deals are often difficult to sell politically, as the losers (workers in particular industries) are concentrated and vocal.** Some of the most obvious gains (lower prices for consumers and greater economic efficiency) are spread out and hard to attribute directly, or accrue to large and well-established corporations. Nevertheless,

there has been no conversation about what to do in Europe and the United States to assist and compensate those likely to lose out from new trade deals.

- **The TPP and TTIP should not become ‘walls’ to further countries joining the trade zones, but should be treated as building blocks that could eventually include a wider network of countries and a wider range of issues.** Twenty-first-century issues such as reform of the financial system and digital economy should be discussed in order to design a truly ambitious framework for enhanced cooperation.
- The West needs to be prepared to deal with the consequences if the TPP and TTIP do not go through. **If the TPP is not successful, it is likely that the Chinese-led Regional Comprehensive Economic Partnership (RCEP) will be completed instead.** If both American-led deals fail, then the rules of trade will be written by others to the detriment of Western interests and norms. Time is running out: the United States and Europe should capitalize on their economic dominance to move forward with TTIP negotiations before the economic balance of power shifts eastwards and becomes less controllable.

### The rise of China, India, Brazil and others: what does it mean for the West?

- Although economic performance in many BRIC countries is weakening, China and India have been described by some as brilliant success stories. The last generation has seen the largest escape from poverty in human history, largely thanks to economic growth in China and India.
- All the BRICs face major structural challenges. In some cases, their initial economic growth was due to a one-off shift in income from some countries to others, not a long-term change (in Brazil and Russia, this was due to commodity availability).
- **While hard power rises with GDP, soft power rises with GDP per capita.** For this reason, most of the emerging countries remain far behind the West in terms of soft power, and it will take decades for the likes of China and India to catch up despite their high GDP growth rates.
- Total economic convergence is rare. South Korea, Singapore and Chile are unique examples. Many emerging economies become stuck in the middle-income trap, with a GDP per capita of around US\$14,000. One of the successes of the European Union is that for decades it has efficiently aided the convergence of member states’ economies.
- **Western policy-makers should be ready for a Chinese economic collapse, rather than simply anticipating endless growth.** Although China continues to grow (albeit at a slower pace), it faces huge underlying challenges. These include an unsound financial system, misallocation of capital, weak banks, an absence of policy levers and poor demographics. China also lacks an adequate social safety net, so it is quite possible that a crisis could lead to nationalism or chaos.
- **‘Straight-line thinking’ also should be avoided when assessing prospects for the global progress of democracy.** There is an assumption among Western policy-makers that democracy will eventually flower in all emerging economies. However, recent evidence suggests that democracy is weakening in some countries with established democratic structures and that prospects for democratization are deteriorating in other, more authoritarian states. Egypt, Iraq and Thailand provide vivid reminders that democratization seldom makes exclusively linear progress.
- **Foreign direct investment (FDI) from China and other economies into smaller European countries may be a challenge for Europe.** It could give investors political influence and add to the pressures impeding consensus in the European Union. FDI in the eurozone can highlight different foreign policies: while China follows a more business-oriented approach in its decision-making, Russia follows a more political and strategic approach. That

said, the West had similar fears about Japanese investment in the 1980s, yet these proved to be overblown.

- While there are challenges to working with China, doing so can also be highly effective in some cases. For example, the bilateral climate change deal with the United States in 2014 demonstrated that China can make real progress in collaboration with Western powers.

### The future of transatlantic economies

- **Fundamental weaknesses remain in the transatlantic economies.** In the United States, boosting labour force participation, repairing household finances and addressing inequality are key challenges. Productivity growth remains elusive both in America and in Europe. While economic growth has returned, Europe has a particular problem with weaker economies, such as Greece and Spain, and will struggle to maintain the cohesiveness of the European Union.
- Finding a solution to growing populism, particularly in rural areas, is difficult due to the lack of policy options to deal with inequality. A lack of resources means that state-led solutions are hard to provide in rural areas and industry is not present there. As a result, the rural–urban divide is often more relevant than the national one to understanding differences in political perceptions in Europe.
- European countries and the United States do not share the same political culture to address the issue of inequality. The tolerance for economic diversity is higher in the United States than in most European societies, which can also explain the different political implications of the economic crisis.
- Growth alone is not the answer to current challenges. The work of French economist Thomas Piketty and others has highlighted that growth is often very unequally concentrated. The United States and Europe need quality economic growth that produces jobs, increases living standards and fosters meritocracy.
- Geopolitical risks loom large for Europe. A revanchist Russia, rising instability in the Middle East and potential European fracture are all very real concerns. The United States is less vulnerable to geopolitical shocks for a variety of reasons, including its geography and growing energy self-sufficiency.
- Productivity growth is crucial if Europe and the United States are to enjoy strong long-term economic growth. However, this is difficult when many politicians are focused relentlessly on the business cycle.
- **Transatlantic powers should remain wary of ‘weaponizing’ economic tools in the pursuit of diplomatic or strategic agendas.** The excessive use of economic and financial sanctions could be counterproductive, as it could strengthen alternative systems. Similarly, TTIP has not been formulated as an ‘economic NATO’ for protecting transatlantic economies against an enemy; its use for strategic purposes should not be overemphasized.