The Group of Seven and Political Management of the Global Economy

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IV CONCLUSIONS

The G7 is often decried as a failure because it has done so little to tackle problems such as slow growth, high unemployment, and exchange rate volatility in the 1990s. Bergsten and Henning criticize what they call the G7's "new consensus on inaction", with G7 countries claiming to be powerless in the face of capital mobility and tacitly accepting a "nonagression pact" whereby each refrains from criticizing the others's policies in return for freedom from foreign criticism of its own policies.[38] But from a perspective that celebrates the global spread of market principles, the G7 might well be considered a success. The new consensus favours action to reduce government management of private market economies and to submit governments more clearly to the discipline of private market pressures. It explicitly eschews interventionist and Keynesian responses to such problems as high unemployment and currency instability, in favour of liberalization and reregulation to make markets work more efficiently. The only regulation favoured by this new consensus is prudential regulation to protect the health of the international financial system, not regulation to prevent international financial instability from disrupting other sectors of the global economy. Discussions in the G7 have helped to forge this neo-liberal consensus, to articulate it, and to spread it to countries outside the G7, even though the origins of this consensus are much broader.

Assessed in light of actual global economic problems, however, the G7 has been a failure in the 1990s. The G7 has promoted the expansion of international markets but has neglected action to protect societies from the negative consequences of unbridled market expansion. It has rarely engaged in active macroeconomic policy coordination to eliminate international imbalances; it has done little jointly to promote global growth in a context of slow growth and high unemployment; it has not cooperated effectively to stabilize exchange rates; and it has rejected international financial reregulation as a means to reduce harmful currency speculation. The economic performance of most G7 countries has been weak in the face of this inaction; growth rates have been low, unemployment rates have been high (except in the US, where unemployment is low but real wages for many workers have fallen), and there has been a regressive redistribution of global income and wealth.

What accounts for the weakness of active political management of the global economy at the G7 level? Neo-liberal theory claims that active political management of the economy is harmful and is no longer viable in a context of open international markets. But this claim ignores evidence that collective political action can have positive effects. In the area of exchange rates, more active coordinated intervention is possible and could have a stabilizing impact. Some limits on speculative capital movements are also possible, although the difficulties of implementing highly effective restrictions should not be underestimated. The ability of the United States to stimulate global demand, and the modest reflationary impact that international pressure has had on Japanese macroeconomic policy, both suggest that active macroeconomic policy coordination to stimulate growth and correct international imbalances is possible. The practice of governments has often been less orthodox than G7 rhetoric, and unorthodox practices are not always unviable.

The obstacles to political management of the global economy therefore are political, not technical. Capital mobility has made macroeconomic management more difficult, but not impossible. The neo-liberal ideology that dominates G7 discussions is itself one of the key obstacles to action, as it suggests that there is no alternative to orthodox macroeconomic policies and neo-liberal, market-oriented restructuring.[39] The recent replacement of right-of-centre governments with nominally leftist governments in Britain, France, and Germany could challenge the dominance of neo-liberal ideology at the G7 level, though the international policy stances of the first two of these governments have not been notably less orthodox and market-oriented than those of their predecessors. But effective interference with international capital markets generally must be coordinated, given the severe international market pressures that face any government that unilaterally diverges from neo-liberal norms. To date the US has blocked coordinated efforts to directly manage short-term capital flows and G7 exchange rates, while its proposals for coordinated macroeconomic expansion have been rejected by Germany and other G7 governments which favour more conservative monetary or fiscal policies.

The 1990s also marked a decline in the success of American efforts to get foreign governments to alter their macroeconomic policies in line with American preferences. While the US had been able to persuade West Germany and Japan to reflate their economies in the late 1980s, it met greater resistance in the 1990s. This reflected some erosion of US influence in Europe due to the end of the Cold War and the increasing European focus on regional policy coordination (see below), but American credibility and influence was also eroded by the failure of earlier administrations to fulfill commitments made in earlier G7 meetings. US demands also represented an unprecedented intrusion into what had previously been considered domestic policy, and as US-Japanese negotiations revealed, this intrusiveness poses a serious obstacle to policy coordination.[40]

From a broader perspective, however, the US has been remarkably successful in promoting its ideological vision of a market-oriented society with modest government intervention. The G7's adoption of this view has been sweeping. Even the difficulties the US government has experienced in persuading foreign governments to reflate is linked to this American success, since open capital markets make it more difficult for governments to adopt the stimulative macroeconomic policies the US often favours.

Closely linked to the declining ability of the US to get its way in the G7 is the development of macroeconomic policy coordination in the European Union. Especially since the 1991 Maastricht Treaty, the three continental European members of the EU (Germany, France, and Italy) have been preoccupied with monetary, fiscal, and exchange rate coordination within the EU. Potential participants in EMU have been motivated in part by the desire to create a zone of relative stability in Europe that would provide some insulation from instability emanating from the United States and Japan. The governments of these European countries therefore have not lost interest in political management of markets, but have pursued it through their regional institutions rather than at the G7 level — again, in part because of their disillusionment with past attempts to coordinate policies with the United States. The success of regional coordination in stabilizing

exchange rates and insulating continental Europe from recent international financial crises has encouraged a downgrading of G7 policy coordination by the continental European members. But the orientation of political management of macroeconomic issues in the EU to date has been overwhelmingly deflationary, and this has contributed to the poor performance of the European and global economies in the 1990s. Regional policy coordination in the EU has already meant that the G7 has become more focused on the ACCs' relations with emerging market and developing countries.

Finally, one should note that the very convergence of national macroeconomic policies around orthodox norms meant that payments imbalances among the G7 countries generally were less serious in the 1990s than in the previous decade. Many of the problems facing G7 countries in the 1990s are common national problems rather than inter-national problems, and thus generate less immediate need for international policy coordination. One possible exception to this generalization is the problem facing Japan in 1998 (as this chapter was being written); if its recession deepens, its trade surplus with the United States will grow and the deflationary impact on the rest of East Asia will increase. Dramatic crises such as a collapse in world stock market values, or the liquidation of overseas investments by Japanese financial institutions seeking to cover losses due to bad domestic loans, could trigger a coordinated G7 response.

Even though the potential for policy coordination remains, in the 1990s the G7 has favoured only one aspect of what Karl Polanyi called the double movement of history. The G7 has acted to promote the expansion of markets across national borders, but has done little to protect societies from the negative consequences of that expansion. This is perhaps most obvious in the case of exchange rates, where the G7 has done nothing to tame the costly instability and economic distortion generated by private foreign exchange trading. Continued inaction in this area will pose a serious threat to the maintenance of a liberal global economy, as more and more societies are disrupted by speculative excesses. Over the next few years, the losses that western banks and hedge funds have experienced as a result of reckless EME crises are likely to lead to less reckless investment practices and to modestly stricter prudential regulation of these activities. These changes may dampen short-term instability, but will do nothing to temper the deflationary pressures facing EMEs and the world economy. Similarly, without Japanese and European contributions to global demand stimulus, the problem of the growing US trade deficit will worsen, bringing with it threats of further instability and American protectionism.

If nothing else, the pattern of G7 action and inaction indicates that the double movement is not an automatic tendency, but rather is an intensely political process. Political management of the global economy in the interests of stability, security, and prosperity for society as a whole needs to be based on a credible alternative to the neo-liberal agenda, and it is difficult to see one at present. The stagflation of the 1970s undermined traditional social democratic strategies, and the pressures of international markets make it difficult for individual governments to adopt policies that diverge from the orthodox consensus. The G7 process has played an important role in developing the view that there is no alternative to orthodox macroeconomic policies and neo-liberal, market-oriented restructuring, through peer pressure and communiques that outline this

view authoritatively. Problems such as those today in Japan and East Asia may well generate ad hoc policy coordination. But significant changes in the direction of stronger political management are likely to occur only in the face of crises big enough to coallesce all of the diverse strands of contemporary opposition to globalization around an as-yet unenvisioned alternative model.

We also need to consider the implications of the pattern of G7 (in)activity for the problems of governmental legitimacy and democratic accountability. The G7's activities have seriously undermined democratic accountability in macroeconomic policy making. The trend has been to insulate meetings of G7 finance ministers and central bank governors from democratic influences by, for example, separating that process from the meetings of the G7 (now G8) heads of state or government. As demonstrated by debates surrounding the 1995 Halifax summit, top political leaders are more sympathetic to interventionist measures such as the Tobin tax than are finance ministries and central banks, and the latter want to control the process to prevent serious consideration of less market-friendly possibilities.

Government legitimacy has also been undermined by the generally weak economic performance of most G7 countries in the 1990s. The poor electoral performance of incumbent governments and growing popular alienation from the political process in many G7 countries are indicators of a legitimacy problem. But instead of trying to enhance legitimacy by direct interventions to improve economic performance in areas of greatest popular concern (by, for example, stimulating demand and growth), the G7 has tried to make subordination to international market pressures legitimate. G7 communiques continually repeat the idea that there is no alternative to orthodox, market-oriented policies, and demonstrate an inordinately strong faith in freer international markets as the solution to most international economic problems. These claims do not correspond to the lived experiences of many people in the ACCs, for whom financial globalization has meant increased economic insecurity and growing inequality. Thus, just as the recent proliferation of international financial crises suggests that the G7's approach is not economically viable in the long run, popular alienation suggests that it also lacks long-run political viability.