



**Project on Future Framework for International Governance:
Contributions of the United States, Russia, China and India**

*Carnegie Corporation of New York
Financial Services Volunteer Corps*

Rapporteur's Report on the Second Symposium of the Project¹

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The second and final symposium of the Financial Services Volunteer Corps (FSVC)/Carnegie Corporation of New York project on *Future Framework for International Governance: Contributions of the United States, Russia, China and India* was held in Beijing, China, on June 8-10, 2013. It was attended by many of the participants present in New Delhi in December 2012 for the first symposium. This provided continuity to the discussion and allowed a deepening of the conversation. At the same time, the project engaged several new younger participants, seen as thought leaders and policy-makers of tomorrow, who added fresh perspectives to the discussion.

Themes

The Beijing symposium, in line with the project's focus, dealt with a number of major concerns facing four key global powers: the United States, China, India and Russia. Problems facing these countries are often transnational and global in nature; the discussion thus dealt with a range of pressing international concerns. Some of these concerns are of existential importance, which makes cooperation among leading nations more pivotal than ever.

Most of the leading themes that emerged in the discussions in New Delhi in December 2012 were present in Beijing six months later. Thus, rather than revisiting all the themes, the group deepened its focus on some of them, also aiming to come up with new insights and possible policy recommendations.

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Some of the principal themes of the Beijing symposium were the following:

(1) The world today is characterized by the difficulty of both “knowing” and “doing.” Knowing the nature of a problem and finding the best ways to solve it are difficult, as problems are manifestations of increasingly complex systems, often beyond the ability of an individual or even an institution to comprehend in all aspects. Unintended consequences are an increasing risk of decisions in such a system.

Doing--acting on existing knowledge and policy insights, for instance--is also challenging, because of opposition, limited resources and capacity, and other implementation issues. The inherent uncertainty of much human knowledge can also be manipulated effectively by the opposition, as seen, for example, in the case of climate change and global warming.

(2) Challenges confronted by individual countries and societies, and by the world as a whole, are grave, and getting more complex. The mood at the symposium was one of awareness of difficult and worsening situations in a variety of areas. However, there was also recognition that while many of the problems are structural and appear to be intractable, they are also often of human creation and can thus be resolved by application of human ingenuity and capacity for problem-solving. That said, urgent action is required on numerous fronts.

(3) Existing government institutions and their leadership are inadequate to deal with today’s increasingly complex problems. While the approaches to addressing this leadership vacuum will be different in each country, there is a clear common need to strengthen public administration and public-sector decision making.

(4) There is an ever-increasing number of participants in international politics and the international economy. While this is not new, the trend continues. It has to be taken into account, especially when talking about transnational threats such as cyber-security, safety of nuclear technology, or dealing with global pandemics. Many problems require transnational solutions, either creating new transnational institutions and power centers or enhancing the role of the existing ones. On the negative side, actors such as failed states, international criminal networks, pirates, and many others, can play a detrimental role in dealing with some of the international challenges.

(5) In many countries, there is an increasing fusion of domestic politics and foreign policy. The role of information, propaganda and information technology thus becomes crucial for both domestic and international audiences.

(6) There is an apparent breakdown of trust in government and political institutions throughout the world and, to a varying extent, in all countries represented at the symposium. While this state of affairs mostly has not become a broader crisis of legitimacy, there is a growing distrust in governments, politics and politicians, and decision-making processes, which will make finding solutions to problems even more complicated. This applies not only to the United States, China, India and Russia, but also

to the European Union and many of the emerging market powers that experienced protests during or shortly after the Beijing symposium, such as Turkey, Brazil and Egypt.

(7) There is a need for deep structural changes in societies and political systems in order to address the challenges effectively. However, such structural change is difficult to implement. Thus, participants often voiced the belief that it would take a crisis to change the situation meaningfully.

(8) Greater income equality, or at minimum rising standards of living, will be necessary, particularly within countries, in order to promote lasting economic growth.

(9) This expectation of a coming crisis or a series of crises emerged as a strong undercurrent throughout the meeting.

Country Discussion

Since the previous symposium, none of the countries present took significant steps to address the issues of particular interest to the project. Participants from all four countries, with the possible partial exception of China, were pessimistic about the state of their national governments and economies.

In fact, in all countries the prescription is similar: more economic growth and social development are needed. However, to attain improvement in the economic and social spheres, political action is required, while the political process in all systems appears to be broken or at least largely dysfunctional. Policy-making in all of the countries appears to be significantly constrained, and often ineffective.

The United States

In the United States, there is no consensus on addressing major issues of the day, either among the political classes or in society at large. In late 2012, President Barack Obama was reelected to a second term with a strong mandate. However, his second term so far has failed to produce major policy changes, to a large extent due to vehement opposition from the Republican Party, which controls the US House of Representatives. There was constructive movement toward the so-called “grand bargain” between the political parties on issues of fiscal policy (which was expected to include a deal on decreasing the national debt and possible changes to the tax and entitlement systems); both sides are likely to want to reach such a bargain, in part to end the spending sequester now in effect. However, in April 2013, this positive momentum ended with the failure of gun control legislation in the US Senate.

Broadly, the incentive for the two parties to compromise is low when there is a realistic chance for a change in majority in one or both houses of Congress in the following election cycle. (Up until 1994, this situation did not exist, as the Democratic Party dominated both houses of Congress for much of the post-war period.) This results in a perverse incentive for congressional leaders to sabotage the other party’s agenda,

whether it comes from the White House or from within Congress, hoping that the failure of the opponent's agenda would lead to electoral gains for one's own party in the next cycle. When the vast majority of congressional seats are considered "safe" for one of the parties due to gerrymandered district borders, incentives for compromise are further eroded. As a result, the United States is experiencing policy and political gridlock on a vast scale.

The US economy is in slow and tentative recovery, characterized by only anemic gains in employment. Still, the US recovery has so far been the best among major industrialized economies, and is impressive when compared with the lackluster economic record of the European Union. Among the positive developments is an improvement in the budget deficit, which is shrinking at a more rapid pace than expected. The energy revolution in the United States is becoming a new engine of economic development that will also have a significant impact on US foreign policy. However, total government spending is increasing as a percentage of GDP.

A series of scandals in Washington, DC, connected to possible intrusions by various government security agencies into the private lives and communications of US citizens, has further undermined the already diminished regard for government in the United States. However, confronting the grave challenges faced by the country--whether addressing global warming, dealing with severe fiscal challenges, continuing to overhaul its financial regulation or upgrading its aging infrastructure--will require major government action and thus may force decision-makers in Washington, DC, to reach compromise.

The European Union/Eurozone

The European Union continues to be convulsed by the Eurozone crisis and its many political, economic and social consequences. Although this crisis has abated in intensity for the moment, the pain inflicted on many EU countries--and citizens--is profound. Moreover, few believe that the crisis is definitively in the past. Many structural problems that caused the crisis, for instance, excessive public debt and unsustainable public entitlements, remain and cannot be resolved quickly. All ways of solving the crisis engage domestic politics and notions of sovereignty in member states, making the Eurozone crisis a political crisis to an even greater extent than an economic one.

One troubling aspect of the Eurozone crisis and its impact on the EU is that many issues that require urgent attention from the leaders in Brussels and national capitals are not being addressed, and are growing more pressing. Most important among these issues are:

1. Migration flows, and management of migration policy internally.
2. Separatist tendencies exacerbated by the EU crisis, in particular in Spain, Belgium and the UK, realistically leading to the possibility of break-up of some of the European states.

3. The absence of a coordinated and coherent position regarding the EU's relationship with Russia.
4. Trade issues, for instance the creation of an Atlantic Free Trade Zone with the United States, a project welcomed but not pursued actively by the EU.
5. The EU's relationship with the strategically and economically pivotal Middle East/North Africa (MENA) region in the wake of the Arab Spring, and brewing unrest in some of the region's countries, on Europe's doorstep.

These issues are interrelated and often seen as crucial by both policymakers and the populations of the EU; however, instead of dealing with these issues, governments are consumed with solving iterations of the Eurozone crisis and attendant changes to the political and economic structures of Europe.

One political process that is slowly taking place is the "modulization" of the EU, in which there emerges a variety of levels on which a country can participate in "Europe." Different levels of participation would increasingly entail different rights, benefits and obligations. The concept of "Europe" at present is flexible, and there is a wide variety of "European" regimes, institutions, organizations, and "clubs" that comprise it. The "modulization" of European agreements may offer a way forward for the EU members and others countries within "Europe" to deal with the aftermath of the crisis.

China

The new leadership of China has given hope that it understands the challenges facing China and has some notion of how to address them. Much remains to be seen, however. President Xi Jinping and his associates have decided that the market is the solution to China's economic woes, according to one senior participant in the Beijing symposium. However, in what way the market mechanism can be used to solve China's problems will take time to define and implement.

There are already some visible changes in China. The new regime aims to bring more rationalization but at the same time exercises more control. For instance, there is hope for more comprehensive transparency and order in the judicial system. At the same time, there appears to be more control by the propaganda machinery of the state.

One important area in which there is positive movement is revision to the land law, including eminent domain reform. Ownership rights over rural agricultural land are crucial for evening out the effects of economic development and urbanization; at present, those who have occupied or used rural land could not benefit from its rapid appreciation in value due to antiquated rules and compensation schemes.

On the negative side, China's economy may be entering a period of instability. There are rising costs in the economy, and credit is booming. The country has created overcapacity in various sectors. Addressing a number of likely bubbles in the economy

may be possible only by allowing a crisis to hit and bubbles to burst. The need for structural reform is profound, and may only come out of a crisis.

The new leadership has termed the current economic situation “unbalanced and unsustainable,” implicitly criticizing the previous regime. The challenge it is facing is how to create new sources of growth.

It has started by eliminating layers of government approvals. It is also likely to enhance its focus on eliminating corruption. It should be remembered, however, that the Chinese central government is very small--around 50,000 people constitute central organs of power--and thus its capacity to oversee and manage the entirety of the economy is limited. There are, however, tremendous innovative capacities in local government that can prove beneficial.

At the same time, there is a growing call by society to rebalance the state’s priorities. Air pollution in Beijing and other major urban centers is many times over the ranges that are considered safe. Chinese citizens, especially the increasingly prosperous middle classes, may be willing to sacrifice one or two percentage points of GDP growth for cleaner air or better food and water safety controls.

US-China Relationship

Presidents Obama and Xi were meeting in California while the Beijing symposium was taking place. According to one Chinese participant, China’s objective is to have a new configuration for the bilateral relationship, which would be a “great power relationship” based on three principles:

- (1) Not denying each other’s ideology;
- (2) Not threatening each other physically; and
- (3) Cooperating on global governance.

India

India is not likely to see much positive movement until the next elections in 2014, when Prime Minister Manmohan Singh will be replaced. In the meantime, there are worsening economic indicators, and policy making is generally ineffective.

The days of automatic growth are over. However, the country is not moving away from its hugely expensive social programs, while economic mismanagement and corruption continue to be major and in some instances growing problems. The FDI environment in the country is problematic. For society at large, food price inflation is likely to be a key concern moving forward, as big dietary changes are underway in India. Overall, the picture in the country is not positive.

There is growing popular discontent with corruption and lack of accountability of the political class. Major protests against corruption and violence against women have

shown the new vibrancy of India's civil society, as well as growing popular pressure for change.

An urgent need for India is to have independent regulators in a variety of spheres of government and the economy. The Reserve Bank of India (RBI), India's central bank, has generally enjoyed a high degree of independence. However, there are efforts to make it more tied to the Ministry of Finance, eroding its independence. That is a move in the wrong direction. The country needs more independent regulatory authorities and better economic management.

A free press and an independent judiciary are two of the positive elements of India's social and political system, and ones that will prove useful during the elections and the next stage of India's development.

Russia

In 2013, Russia's political system under President Vladimir Putin has rapidly grown ever more rigid and conservative. Many of the Russian participants expressed concern and pessimism about the country's direction. The current trend in Russia is for increased state presence in the life of the country in all of its aspects, be they political, social or economic.

In the economic sphere, there is increasing state presence (which has already been considerable). There is ongoing movement by the state, via state-controlled corporations, into new spheres of the economy, for instance, telecoms. A new tax regime forced several hundred thousand small businesses to close in early 2013. Although there may be some positive effects to Russia's integration in some international organizations, such as its accession to the OECD, it is likely to be offset by negative developments in the country's domestic environment.

In the political and social spheres, the state and particularly the presidential administration are eliminating any possibility of political or social action that they see as being opposed to the regime. There is a multitude of restrictive new laws and regulations. To cite a few examples, they force civil society groups and research institutions that receive some funding from abroad to register as "foreign agents," a term that has connotations of spying; actively discriminate against categories of citizens (most prominently, the gay community); and impose conservative, often Russian Orthodox values on the society at large. The sudden emigration of Sergei Guriev, a leading economist and public intellectual with close connections to the government, has demonstrated that the expert community can also easily fall under attack by the conservative wing of Russia's government, often associated with prosecutorial and secret services. In general, Putin's actions are leading to the destruction of the institutional integrity of Russia's government and society, and to a decreasing pool of talent to call on during the coming years.

It is not yet clear whether this tightening of political controls in Russia comes primarily from President Putin's sense of weakness and fears of a potential crisis, or from some other source. It is likely, however, that developments in Russia over the past year have created more, not fewer, risks and sources of uncertainty for Russia's not-very-distant future.

The Global Financial Sector

The world is still dealing with the consequences of the financial crisis of 2007-2009, while in some countries, such as China, possible signs of new financial difficulties are beginning to appear. Yet it is too early to talk of lessons from the previous financial crisis; it is not far enough in the past, and cannot be considered definitively over.

The recent crisis was caused in large part by an oversupply of money/liquidity and insufficient banking supervision. Unfortunately, both of these conditions are still present.

The world is experiencing a slow economic recovery, which Christine Lagarde, the head of the International Monetary Fund (IMF), has termed a three-speed recovery. Emerging markets have been doing mostly better than Western economies, but not robustly. The United States is recovering to a significant extent because of the Federal Reserve's liquidity policies, thus raising questions about the sustainability of its recovery path. European growth has been problematic, with multiple tiers of recovery and policy-making appearing within the EU and the Eurozone (with some countries being mired in deep recessions with catastrophic levels of unemployment).

Globally, financial regulation is expanding. There are now tougher capital and liquidity standards. However, new regulatory regimes, such as Basel III and rule-making under the Dodd-Frank Law in the United States, are extremely complicated, running to hundreds and thousands of pages of technical instructions. As a result, the costs of compliance are becoming much higher for financial institutions globally. Profitability of the world's banking sector is likely to decline. Already, the financial sector is experiencing extensive realignment and restructuring. While banks again may become more tightly linked to growth in the real economy, which would be positive, higher operating costs and regulatory pressures may well limit what banks can do.

Thus, countries and governments, both nationally and internationally, need to ask, what do we want our financial sectors to do? And, what kind of supervision and regulation helps to achieve this goal?

In this context, the reform of global financial infrastructure is an urgent issue. The world needs strong global institutions for regulation and supervision. Business and finance know no borders. While business and financial institutions are truly international, regulation continues to be national or, at best and rarely, regional. There is a need for reform.

One suggestion in this context is to enhance the role of the IMF and to reform its governance to make it more representative. This may be problematic, due to likely US opposition. The United States is generally unwilling to cede its sovereignty and has a strong preference for passing domestic legislation that has wide-ranging and often distorting effects on other jurisdictions, without consultation with foreign authorities.

Another key issue in the financial sector is social equity and equality. Financial inclusion is increasingly a priority globally, including in countries such as India and China. For instance, in India 50% more people have cell phones than bank accounts. New technologies should enable more people to obtain access to useful banking services. Alleviation of poverty and inequality is an especially urgent task in a world where climate change and attendant crises are likely to affect some of the poorest areas most severely.

A related concern is the size of the shadow banking system, and gray/informal economy, globally. Financial inclusion could help limit the expansion of the shadow banking system, even if increased regulation globally provides an incentive for it to flourish. According to a recent Financial Stability Board estimate, the global size of the shadow banking system in 2011 was USD 67 trillion, including USD 23 trillion in the United States and USD 2.2 trillion in China.

Energy and Climate Change

There is now scientific consensus that climate change/global warming are indeed taking place. An increasing number of disruptions, unusual weather patterns, and catastrophic events are likely to occur. The exact nature and scale of these disruptions are not yet known, but it is probable that events of the magnitude of Hurricane Sandy in the United States will be happening more often.

In the world today, there are four basic ways to generate power: hydro, nuclear, carbon (coal, oil, gas), and renewables. If the assumption is correct that there is climate change/global warming, there is no other practical and economical way to meet the world's growing energy needs (without aggravating the global warming problem) than to expand nuclear power generation rapidly on a global scale.

Such an expansion of nuclear technology should be accompanied by transnational efforts to control and track nuclear fuel, as well as to monitor proliferation and safety regimes. This would require setting up new international institutions with strong international mandates.

The energy equation is changing in multiple countries simultaneously. The United States is on track to become self-sufficient in energy within a short period of time. In China, a massive expansion of nuclear power generation is underway. In Russia, the giant state energy companies have generally failed to catch up to the changing global energy landscape. Russia may consequently need to adjust its strategy in a situation

where its gas is becoming expensive to produce while the security of demand that previously existed is no longer there.

There are new technologies being developed for safer nuclear power generation; however, it is not clear whether and when such technologies may become available. China's role in coming up with the next generation of nuclear technologies is yet unknown, but could prove crucial.

A shift away from carbon power generation is going to require setting an international price on carbon. So far, there has been resistance to move in this direction from many quarters; it is possible that some major crises and disruptions would be required for global consensus to shift rapidly in the direction of limiting carbon emissions and taking urgent measures to change the global power generation regime.

In the meantime, there are also concerns regarding possible catastrophic scenarios. In particular, large amounts of methane hydrates might be released into the atmosphere as global permafrost melts; should that happen on a large scale, it could lead to human extinction within a short period of time.

Crises of Tomorrow

The group devoted much attention to the likely future crises to be confronted by the world. While there may be different philosophies as to what constitutes a crisis and how to deal with crises, some challenges are clear and could present a threat to all of the key countries.

Crises are unavoidable; there will definitely be another crisis. However, humanity and the expert community do not have a good track record of predicting when a new crisis will hit and what form it will take. There are several areas on which it would be reasonable to focus, both to increase awareness and to be better prepared when one or several of these problems arise.

(1) The next financial crisis

The next financial crisis is likely to take place before other major disruptions occur. In fact, the previous financial crisis has yet to end definitively: the recovery has been slow, and there are problematic areas in the financial systems of all of the countries under discussion.

The problems are exacerbated by the fact that fundamental issues raised by the crisis of 2007-09 are unresolved, and in fact there is ever more intense debate about them. When confronting an economic and financial crisis, is stimulus or austerity most effective? What is the best way to apply banking regulation, without stifling the productive functioning of financial institutions and the banking system as a whole?

The global financial system today is operating under conditions of loose monetary policy and excess liquidity; there are almost certainly growing asset price bubbles. These are the likely seeds of a new crisis.

(2) Global warming events

Disruptions caused by global warming are likely to mount and to have profound effects in multiple countries around the world. The effects of global warming will often be political. Most societies, and especially the poorer ones, are not flexible enough to adapt to the effects of global warming challenges at this stage.

There are going to be increasing numbers of examples of political disruptions caused by climate change-related phenomena. The Arab Spring has been caused to some degree by rising food, particularly bread, prices in the market, caused in turn by a series of bad harvests. The civil war in Syria has flared up after four years of severe drought, which plunged large portions of the population into extreme poverty and hardship. A particular area of concern is Pakistan, where water distribution issues are a source of continued political stress and could lead to violence erupting suddenly should the situation worsen.

(3) Cyber-security

The ability of societies to deal with a large-scale cyber-attack has not yet been tested. However, cyber-security is becoming a major area of concern for institutions and governments worldwide. Some prominent individual institutions, for instance, in the financial sector, experience millions of attacks per year, and disruptions to a country's financial, energy or other vital infrastructure could be potentially catastrophic.

Recent tensions between the United States and China, and the previously alleged attacks by Russia on Estonia (which, in fact, may not have come from Russia), demonstrate the potential for cyber-security issues to cause major international disagreements and potentially broader conflict.

(4) Pandemics

Pandemics and the emergence of drug-resistant strains of viruses are likely to happen with new frequency, and will have to be addressed extremely rapidly on a global basis if the response is to be effective.

Policy Recommendations

The participants in the Beijing symposium, in particular, focused on policy recommendations that stemmed from the discussions. It was agreed at the symposium that seeking consensus among all the participants is not likely to be fruitful, as it is precisely the diversity of views and perspectives that make the Carnegie/FSVC series of

projects so valuable. Some of the policy recommendations that pertained to key areas of discussion were the following.

Financial sphere:

- (1) Reform the governance of the IMF and expand its mandate.
- (2) Change the mandate of the World Bank, making it more limited and focused. Some of the possible new directions would be:
 - a. support clean government/transparency;
 - b. promote sustainable development;
 - c. provide development finance; or
 - d. focus only on the least developed countries, with the goal of poverty alleviation.
- (3) Develop an international information-sharing regime and set of standards for the “too big to fail” or “too big to regulate” institutions.

Legal:

- (1) Produce short briefs on complex international regulatory issues, especially in technical fields such as finance and nuclear energy. Disseminate broadly to foster understanding and sharing of best practice.

Cyber-security:

- (1) Promote the adoption of a UN Security Council Resolution (modeled on UNSCR 1540) on cyber-security, cyber-terrorism, and cyber-attacks.
- (2) Develop an internationally-agreed definition and thresholds for what constitutes a cyber-attack and cyber-terrorism.
- (3) Create a cyber-forensics program under the aegis of the United Nations.
- (4) Develop international agreements on cyber-security, including commitments not to attack vital infrastructure (such as power stations, transportation networks, health centers, etc.).
- (5) Establish hotlines dedicated to cyber-security.

Energy and climate change:

- (1) Develop a regime for assistance and compensation by richer nations, historically most responsible for climate change, to poorer nations, which may be hit the hardest and be least able to cope with effects of catastrophic events.

- (2) Invest in education on climate change and global warming-related disasters.
- (3) Create an international consortium for trading nuclear fuel among suppliers and consumers (countries).
- (4) Conduct internationally-funded collaborative research on new safe and secure nuclear technologies.
- (5) Involve China more actively in nuclear energy regimes.

Concluding Observations

The discussion in this symposium in Beijing was one of the most thought-provoking that FSVC has ever organized, and helped frame complex policy issues in new and illuminating ways. The inclusion of a number of “rising young stars” from each country also contributed to a dynamic exchange of views and provided an important perspective from emerging market countries that have experienced significant change over the past generation.

Participants discussed at length how they could share their ideas, particularly so that they reach policy-makers in each of their countries. Both FSVC and the participants committed to address this important dissemination issue. A number of avenues of dissemination were explored, and several will be implemented on an ongoing basis over the next few months by FSVC in collaboration with participants. They include an expanded webpage dedicated to the symposium and project on FSVC’s website, round-table policy events in Washington and New York featuring symposium participants, and op-ed pieces and longer policy papers by participants.

Problems in the international financial system, energy security and climate change rank among the most complex issues facing the world today; they require the coordination of policies at the international level, and cooperation among the United States, Russia, China and India will prove critical in addressing these issues. While several policy recommendations were developed, the Beijing symposium, more importantly, helped frame key issues, and contributed to building understanding among experts and opinion-makers from numerous countries.

In the face of increasingly complex problems, participants from all four countries noted the inadequacy of existing government institutions and their leadership to deal with the challenges at hand. While the approaches to addressing this leadership shortfall will be different in each country, there is a clear common need to strengthen public administration and public-sector decision making.

There is an urgent international need to transform prevailing approaches to energy production. There is also a need to achieve greater income equality, or at minimum rising standards of living, particularly within countries; this will be essential in order to promote lasting economic growth. Problems in each country’s financial system, and in

the international financial architecture, are closely associated with each of these other challenges, and must be addressed in order to make progress in these other areas. The Beijing forum was able to discuss these issues constructively and candidly, in part, because of the unusual level of trust that has been achieved among participants from the four countries.