

Bruce Gerson: Welcome to Carnegie Mellon Online. For more multimedia from Carnegie Mellon University visit www.cmu.edu/multimedia. Hello, I'm Bruce Gerson and welcome to this Carnegie Mellon University G-20 Podcast. In these interviews, you'll hear from several leading Carnegie Mellon faculty members about some of the issues related to the G-20 summit this September 24th and 25th in Pittsburgh. Back with us today is Lee Branstetter, Associate Professor of Economics at the Hines College. Professor, as you know developing countries have criticized international economic policy making institutions for inadequately reflecting their interests, priorities and concerns. Are these criticisms justified and if so, how might we respond?

Lee Branstetter: Well let me limit response to three very important international policy making institutions; the WTO, the World Bank and the IMF. The World Bank and the IMF were created in the aftermath of World War II; the WTO grew out of the GATT, which was also created in the immediate aftermath of World War II. And there's a sense in which the structure, the location, the leadership and therefore the priorities of these institutions reflect that early postwar balance of economic and political power more than they should today. The World Bank and the IMF are based in Washington, D.C.; the WTO is based in Geneva, Switzerland. The location of these institutions in the U.S. and Europe, respectively, inevitably affects them in subtle and not so subtle ways. Furthermore, ever since their founding, the World Bank has always been led by an American citizen and the IMF has always been led by a European. Now, there's no law that mandates this, but there has been a kind of gentleman's agreement between the rich countries to organize the institutions that way. And they've been organized along those lines for about 60 years. Now you can imagine how the Indians, the Chinese and the Brazilians might feel about this. There are plenty of qualified Indian, Chinese or Brazilian nationals who could, in principle, take a turn at leading these institutions. Now, the head of the World Bank and the head of the IMF do not have absolute power over their institutions. After all, the former World Bank President, Paul Wolfowitz, was basically forced out despite support from the Bush Administration. But the ability of the American president to place such a controversial figure, one with what some people saw as limited experience in the area of economic development, in such a position of international policy making power was a real affront to many people from many countries. And it kicked into high gear a debate about how the senior leadership of these institutions might come to reflect the current balance of economic power in a better way. At market exchange rates, China is now the third largest economy in the world. At purchasing power parity exchange rate, which reflect the low prices of some goods and services in China, it's already the second largest market economy and by any measure, China could be a larger economy than the United States, the largest economy in the world, as early as the 2020's. But given current practice, there's no prospect whatsoever of a Chinese national coming to head either the World Bank or the IMF. It's hard not to see how developing countries would view this as

just patently unfair. In addition to the privilege of appointing the head of these organizations, the U.S. and the EU also exercise power through their ability to influence activity via their voting rights within these organizations. Effectively, the U.S. and the EU hold shares in the World Bank and the IMF based on their contributions to the capital of these organizations. Together the U.S. and the EU constitute a voting block that can, and does, dominate these organizations. Now Japan also has a voice thanks to its financial contributions to both organizations, but Japanese interests are often aligned with those of the U.S. and the EU. The WTO and its predecessor, the GATT, have been a bit more democratic. But only one Director General of the GATT or the WTO has not been from a western country. Everyone else has been from Europe or North America or New Zealand and the current WTO Director General is a European. Now the WTO formerly operates according to a one country, one vote principle, but the real decision making is done informally through consensus and the countries with the biggest domestic markets tend to have the most leverage in these negotiations. Historically, that has put the U.S. and the EU together with Japan in the driver seat. And there are other powerful features of the modern economic system that reflect, perhaps unfairly, the early postwar economic dominance of the U.S. The most visible example of that is probably the international role of the dollar. We now have countries like China complaining about the privilege bestowed upon the United States by virtue of the fact that the reserve currency on which the world financial system is based, is minted by the U.S. and under the control of the Federal Reserve and the U.S. Treasury. Now, by the way this so-called exorbitant privilege was noted and criticized by the great British economist John Maynard Keynes who pushed for the creation of a truly international reserve currency in the late 1940s. That push didn't get anywhere then and in the immediate future, I don't think the push for a different international currency system is going to get anywhere either, which does leave the United States with a position of special privilege and power. Now, what we could we do about this? Well, we could ask the Americans and the Europeans to let someone else take a turn running the World Bank and/or the IMF and the next Director General of the WTO could be someone from a developing country. With the agenda change, if say the Indians could pick the next head of the World Bank, I think it would. I think there would be more focus on things the developed countries do that really work against the economic interests of developing countries. Agricultural subsidies and agricultural protection really do work against third world interests in ways that most Americans just don't understand. The presidency of the World Bank would be a useful platform from which to shine a light on these things. Another big issue is immigration. There are respected economic studies, controversial ones, but respected ones, that show that a substantial increase in the right of workers in developing countries to seek employment in developed countries would have a much more positive impact on the welfare of the world as a whole than any liberalization in trade currently on the WTO agenda. The Europeans and the Japanese have refused to put immigration on the international policy agenda, but this will be harder to ignore under an Indian presidency of the World Bank. Finally, poor developing countries like India tend to view the climate

Interviewee: Lee Branstetter Interviewer: Bruce Gerson / Changing the WTO, World Bank and IMF
5.mp3

change debate and the tradeoffs between economic growth and reducing greenhouse gas emissions in a very different way than new developed countries. For this to happen, America and Europe would have to voluntarily relinquish a privileged position of power that they've held for six decades. Once they relinquish this power, they would not get it back. So it surely involves risks, but at some point, I do think this has to happen otherwise the currently dominant economies would run the risk of delegitimizing the very institutions on which we rely to coordinate economic policy in an ever more dependent global economy.

Bruce Gerson: Thank you Professor Branstetter for your time and your insights. This has been a Carnegie Mellon University G-20 Podcast. Thank you for listening.

End of Changing the WTO, World Bank and IMF 5.mp3