



C. D. Howe Institute – Sylvia Ostry Lecture

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Ladies and Gentlemen:

It is a great honour to deliver this year's Sylvia Ostry Lecture at one of the world's epicentres of public policy enlightenment. I stand in this forum with a sense of humble enthusiasm and tempered pride. Thank you so much for this invitation.

Before I start my presentation, I would like to express my admiration of Sylvia Ostry. Sylvia is a natural visionary. Her mind and writings are very often one step ahead of their time. That's why the titles of many of her speeches and papers start with the phrase "The future of..." Sylvia's passion for public policy and her "Copernican" attitude towards economics have empowered her with a special ability to see "the governing dynamics" of globalisation — to borrow the expression from Ron Howard's film "A beautiful mind". For these and many other reasons, like our common quest to make globalisation work for all, and our shared OECD roots, this Lecture has a special meaning to me.

These challenging times demand new blueprints. I get the impression that throughout the current financial and economic crisis we have been much better at explaining what has happened, than at pointing a new way forward. In the coming years, the world economy will need a much more solid connection between public policy and the public for which policy is made. The spinal cord of that connection can be summed up in one question: What kind of world economy do we want to create?

1. Finally, a way out of the crisis! *But where are we going?*

Let me start by asking a simpler question: What is a crisis? What is the essence of this concept? Failure, opportunity, paralysis, metamorphosis? What does it mean when it

involves the whole world? Why has it now become a cliché that “a crisis is a terrible thing to waste”?

During the past four decades, we have lived through 88 financial crises. What have we learned? Why are they so recurrent? Is it possibly that our solutions are constantly planting the seeds of the next crisis? Is it maybe that we hadn't fully realised the increasing importance of global economic interdependence? Is it because we were trying to fix a global challenge in a fragmented and narrow manner?

But, perhaps most importantly, will this crisis help us do things differently? Carlos Fuentes, a writer, who comes from a country that has had its fair share of crises, — my own country, Mexico —, used to say that “a crisis is only catastrophic if it doesn't produce an offspring that surpasses it and redeems it”.

The current crisis is a financial, economic and social catastrophe. Trillions of dollars have been knocked off the value of stocks, pensions and balance sheets. Public finances will take more than a decade to recover their lost strength. Unemployment has reached record levels and threatens to become structural in many countries. Poverty is on the rise and world hunger has reached a record 1 billion people. The costs of our failures this time are huge.

This increases our responsibility to learn our lessons and do our homework. What we are living is more than a crisis; it was massive regulatory failure; massive supervisory failure; massive corporate governance failure; massive risk management failure. We are also witnessing the breakdown of the previously accepted notion that financial markets tend to equilibrium; that they tend to regulate themselves. Thus this transition is giving us a historic chance to build something better.

In fact, we are already learning, debating, questioning; we are looking for answers, for solutions. We are responding in an increasingly coordinated way. Since the Lehman-related detonation of the crisis, back in September of last year, we have put together the largest co-ordinated response to an economic crisis in history. Governments have reacted decisively, with a fiscal boost on a massive scale, and central banks around the world have made unprecedented efforts to lower rates to practically zero, stabilise the financial system, avoid panic and provide liquidity.

The crisis has fostered an unprecedented degree of international cooperation and coordination. A new global architecture is being born. The emergence of the G20 as the premier economic coordination body has been one of the most important achievements. Another dramatic change is the participation of major emerging market economies in such a global economic policy coordination.

Never have the heads of government or economics and finance ministers of major economies, developed and developing alike, spent so much time talking and developing coordinated responses. And never have international economic organisations been in such a close coordination with each other and with governments, exchanging views, blending experience, building shared solutions.

This has brought some good results. The global economy now seems to have successfully stabilised, with downward trade and output curves at least flattening at present. We are starting to exit the crisis and this is great news; but, where are we going? Exit yes; but exit to what? What kind of world economy do we want to build? What are the fundamental changes that we need to put in place after all this fire-fighting?

And are we sure we are not already planting the seeds of the next financial crisis? Some developments require attention in this regard. One is that countries in which the crisis emerged are in a very different position to the Asian region and emerging markets more

generally. When rates are low (and zero in some cases) a carry trade is set up to search for better yield and asset appreciation in non-crisis countries with better fundamentals. This is leading to massive capital inflows and new “bubbles” are forming in these regions.

Another issue worth noting is that countries like Australia, Canada and Spain did not need to make capital injections to rescue banks; yet they had access to the same derivatives and structured products; had to deal with the same credit rating processes; participated in the same Basel rule issues; dealt with the same accounting standards; had the same bonus systems for bank ‘high-fliers’ and they often had less capital than their counterparts elsewhere). So other forces were certainly at work, and these other forces need to be on the agenda too. A key issue here is understanding what banks do. All sound banks are the same; all unsound banks are unsound in their own special way. The OECD is focusing on these issues and addressing fundamental questions such as whether a more structural separation should be encouraged in financial groups between commercial banking and other parts of the group. In a way, this would serve to keep the credit culture and the equity culture separate, so that government deposit insurance does not end up cross subsidizing high-risk market activity, and so that contagion and counterparty risk can be reduced.

This reminds me of the shortest story ever written, by that wonderful writer from Guatemala Augusto Monterroso. The story reads: “*Y cuando despertó, el dinosaurio seguía estando ahí*” (And upon waking, the dinosaur was still there). The same applies to us now. We might be waking up from this nightmare, but our structural challenges are still there; many of them have grown to the size of a dinosaur. And it is precisely with the choices we make while addressing these challenges that we can engineer a more stable future, a more resilient, sustainable and inclusive growth.

2. Reinventing the future: a stronger, cleaner and fairer global economy

As our attention remains fixed on the not yet fully tamed global crisis, pressures are beginning to be felt on longer-term questions like fiscal and environmental sustainability, structural unemployment, growing poverty and inequalities. Indeed the whole direction of progress is at stake. “*Ayez de l’avenir dans l’esprit*”, Talleyrand used to say.

Our OECD Ministerial Council meeting, last June, has set the shared objective of our 30 member governments in terms of “building a stronger, cleaner and fairer world economy.” This calls for renewed emphasis on a number of fronts.

a) *We need a stronger global economy.*

Our global economy must be based on a more robust structure that can deliver stable, long-term and more inclusive growth. At OECD, we think we have a fairly good understanding of the right policy framework that can drive such a growth. For several years now, through our annual work on “Going for Growth”, we have been providing detailed recommendations based on systematic, in-depth analysis of structural policies and outcomes, relying on a set of internationally comparable indicators, covering labour markets, education, competition, regulations, innovation, health and many other policy areas.

In a potentially far-reaching decision, the G20 agreed to exchange and assess information about their respective macroeconomic and structural policies in order to avoid future crises and strengthen future global growth.

Thus the Pittsburgh Summit adopted the Framework for Strong, Sustainable and Balanced Growth. The OECD, with its longstanding experience in economic peer review and cross-disciplinary analysis of policy interactions, is ready to help. The OECD is proposing to adapt our Going for Growth framework and expand it to cover all G20 countries. This means agreeing on performance indicators and policies relevant for advanced and emerging economies taking into account context and institutional setting. It also means assessing the systemic impact of policies and looking at the contribution of structural reforms to deal with global imbalances.

b) We need a cleaner global economy.

Climate change is the greatest and most immediate threat we face. It is destroying our only planet at an accelerating pace. If we continue with the same policies, global GHG emissions would increase by about 70% by 2050 and continue to grow thereafter. This could lead to a rise in world temperatures of 4°C above preindustrial levels, and possibly 6°C, by 2100. Such a rise would translate into an environmental, economic and human disaster.

Achieving the ambitious climate targets of limiting global temperature rise to 2°C is affordable. In fact we estimate that it would cost just about one-tenth of a percentage point of the world's annual GDP between 2012 and 2050. This would mean a 4% cumulative reduction in GDP in 2050 compared to a scenario where no policy action is taken. Bear in mind that, over the same period, world GDP is projected to grow by more than 250%.

I feel the political climate is changing. The OECD Ministerial Green Growth Declaration (June 2009) and the G20 agreement to phase out subsidies to fossil fuel energies are encouraging signs. We should at least be able to agree on a framework and set a blueprint for action during the upcoming COP15 Climate Change Conference of

Copenhagen. This brings to mind Jan Arthus-Bertrand “It is too late to be pessimistic”.¹ We only have 10 to 15 years “breathing space”, so we have to act fast. “When skating over thin ice, our safety is our speed”, as Ralph Waldo Emerson reminded us.

But we also want the economy to be cleaner in an ethical sense.

I am sure many of you have heard about the recent global convergence process in the field of tax compliance. I am referring especially to the recent expansion and strengthening of the Global Forum on Transparency and Exchange of tax Information and the ending of the era of banking secrecy, allowing countries to fully enforce their tax laws and protect their tax bases. Since April, over 100 tax information exchange agreements have been signed and over 60 tax treaties have been negotiated or renegotiated to incorporate the now globally endorsed OECD tax transparency standards.

What allowed this remarkable achievement – one of the tangible results in global cooperation since the onset of the crisis – is the juxtaposition of two things: strong political clout and pressure from major economies working together in a G20 context, combined with longer-term, fact-based policy standards development in an OECD setting. One without the other could not have delivered this spectacular result. The model could very well be used for other areas of international cooperation, like climate change.

c) And we also need the new global economy to be fairer.

“Are we growing unequal?” we asked months before the crisis. The last global boom was associated with a growing concern in many countries that the bottom or even the middle sections of the income distribution were not sharing in its fruits. Unfortunately, Canada was among them. Then came the recession and, notwithstanding the green shoots, it is

now having its woeful impact on jobs. The numbers are staggering. From a 25-year low at 5.6% in 2007, the OECD unemployment rate has risen to a post-war high of 8.9% in this Quarter. Although the job losses have affected all social groups, it is the disadvantaged people in the labour market – youth, the low-skilled, immigrants, ethnic minorities and those on temporary contracts – who have borne the brunt, as ever.

The crisis should not become an excuse to postpone our commitments with the poorest of this world. On the contrary, it is a new, compelling reason to accomplish them. The poorest families of this world, both in developing and developed countries, are at greatest risk from economic shocks. The International Labour Organisation (ILO) estimates that there are 200 million workers at risk of joining the ranks of people living on less than \$2 per day between 2007 and 2009.ⁱⁱ

This financial contraction will put a tremendous pressure on budgets in poor countries. Innovative financing for development is an increasingly important instrument; a complementary way to help developing countries overcome their structural challenges; to help them achieve long-term, sustainable development.

To make the world economy fairer it is crucial that we improve the effectiveness of development aid flows, that we incorporate developing countries into global trade and investment flows. We must also increase our aid for trade support and decrease our agricultural subsidies; strengthen social empowerment through education, and promote fair competition and vibrant innovation systems. OECD is working in these and other areas to make globalization work for all.

To achieve these goals, to be able to build a stronger, cleaner and fairer global economy, we will need a new set of shared values, and we will have to promote four key

instruments for human progress: innovation, open markets, new ways to measure economic and social progress, and enhanced and more inclusive international cooperation.

3. Four catalysts for a better global economy

a) Broader innovation

Innovation is the soul of change. It is not a panacea, but it is the only thing that can shift our production frontier outwards on a permanent basis. And innovation can critically contribute to addressing global environmental problems or open up entirely new sectors of value and employment creation.

We have come to realise that a broader view of innovation is necessary. We see innovation involving more “open” practices – firms collaborating with external partners to keep ahead of the game. We seek a better understanding of non-technological innovation. We see innovation becoming increasingly international, with multinational enterprises playing a key role in its geographical location, and emerging economies participating strongly.

As a result, innovation has moved to the centre-stage in economic policy making, and if policy is to play a role in fostering it, a coherent “whole-of-government” approach is required. It is in this context that we at the OECD have embarked on developing a broad-ranging Innovation Strategy. I hope to share its main results at the next Montreal Conference in June 2010.

b) Open markets

International trade has taken a hit unprecedented in post-war history. Total world trade volume has collapsed by nearly 15 percent in the year to the 3rd quarter of 2009. Even if world trade has now stabilised, the last thing we want to do in the present circumstances is to damage further the open trading environment.

There are legitimate fears that policy responses to the crisis may impact on trade. Thus far, governments have been relatively restrained in their use of overtly protectionist trade measures. Overall, governments appear well aware of the folly of such actions. In the area of stimulus measures, there is an indirect impact on trade, and the sheer size of some packages suggests that some measures will have a very large impact, including on trade. But we at the OECD remain focused on this problem: we want to ensure that the policy environment remains supportive of the free flows of trade and investment on the basis of comparative advantage and in response to economic opportunities.

Protectionist pressures can be expected to mount, not diminish –fiscally strained governments will be tempted to respond as unemployment numbers continue to climb. We are monitoring actions that could be taken to ensure that the negative impacts of sectoral subsidies (for example, in financial services, automobiles, and household appliances) and of discriminatory provisions in government procurement initiatives (for example, buy-national requirements) are minimised, and that a retaliatory spiral is avoided. I know this is a particularly important concern to this audience.

We are also keeping a watchful eye on investment restrictions. In a recent joint report to the G20 with the WTO and UNCTAD we concluded that, overall, investment policy measures taken by G20 members paint a reassuring picture. A substantial number of policy changes undertaken in recent months were directed at increasing openness and clarity for foreign investors. I know views on openness to investment vary even within

this country. But here is a clear link to global governance and multilateralism. To put it bluntly, you fear that unilateral action in the auto sector by your largest trading partner can put you in a difficult position. The only way to avoid this is through strengthened global coordination within a multilateral framework.

c) *A new way of measuring progress*

And we wish to develop an understanding of progress going beyond output growth. We need to move beyond GDP as the single yard stick of progress. There is a growing gap between what official statistics tell us about our economies and how people see the conditions in which they live their daily lives. And this gap can be clearly damaging both to the credibility of political debate and action and to the very functioning of democracy in our countries.

The Report by the Commission on the Measurement of Economic Performance and Social Progress, led by Joseph Stiglitz, has made a remarkable contribution. This has been part of a wider process driven, among others, by the OECD. Two weeks ago in Seoul we debated ways to measure the world's well-being, in line with G-20 calls for statisticians to go beyond measuring economic output. As I noted then, the global economic crisis has revealed the growing gap between official statistics and people's perceptions of their standards of living.

Getting our measures of progress and well being right is thus a high priority now. It is essential for the credibility of our public policies and for confidence in government and in democracy itself. It is only with better measurement that we can build better policies and be able to convince the public that our policy action has tangible – and positive – impacts on peoples' life.

d) Enhanced and more inclusive international cooperation

The only way we can build a stronger, cleaner and fairer global economy is through enhanced and more inclusive international cooperation. The global governance architecture must reflect a changed world reality. The emergence of innovative schemes like the Major Economies Forum (MEF), the Heiligendamm-L'Aquila Process, the G8+G5 or the G20 suggests a growing realisation that we cannot build a stable global economy without including developing countries in the decision-making process.

The multilateral perspective needs to be represented “around the table”. This is the job of international organisations (IGOs), with their neutral – expert – professional staffs. It is here that the next important weak link in the chain of global governance must be strengthened – cooperation and collective action by a network of IGOs, meaningfully backed by leading economies, paying heed to the advice they have collectively generated.

I am happy to say that we are making progress on this too. Better coordination and cooperation among IGOs was called for by Chancellor Merkel as early as 2007, well before the current emergency. To further this idea I have recently proposed the creation of an Observatory for Policy Coherence, bringing together the IGOs involved in the G20 Framework for Strong, Sustainable and Balanced Growth (IMF, World Bank, OECD, FSB, ILO and WTO), with the objective of improving co-ordination and exchange of information between them, thus making sure that Finance Ministers and leaders will get the best possible advice. Knowing the skills with which my Canadian colleagues usually lead and build international consensus, I am sure that we will be able to move this idea forward in the upcoming Muskoka Summit.

4. A Canadian contribution

Canada has a tradition and a passion for multilateral cooperation.

Canada is one of the most “well-connected” countries in the world. Very few other nations participate in such a far-reaching network of international organisations with so much conviction and faith. As a recent paper by Tom Keating suggests, Canada’s commitment to multilateralism has earned it a reputation as an inveterate “joiner”, as a reliable and responsible global citizen.

This active participation in multilateral organisations is based on wide public support, to such an extent that it has been considered by some as a symbol of Canadian identity. As Stephen Lewis, an exemplary Canadian contributor to a better world has put it: Canadians “have a lasting and visceral commitment to multilateralism which is ingrained and endemic to the Canadian character.”ⁱⁱⁱ

The substantial results and the degree of inclusiveness of the previous Canadian Presidency of the G8 in 2002 — where important decisions were made to promote sustainable development, to assist highly indebted developing countries, to help Africa address its major challenges, and to forge a global coalition against terrorism — allow us to be optimistic and to expect a path-breaking and results-oriented summit in Muskoka.

For many years, Canadian statesmen, diplomats, decision-makers, economists and academics have been bringing to the table of multilateral negotiations a collection of ideas, proposals, agreements, protocols, and initiatives to establish an international financial and economic system conducive to sustainable development. With its multilateral network and know-how, its experience on adopting difficult reforms and its growing engagement in promoting an environmentally responsible economic culture, Canada should raise its voice in the international fora and drive change, spreading that very Canadian conception of the world as a team.

Ladies and Gentlemen:

What will we be discussing in ten years from now? Will the planet be entering an environmental nightmare in 2020? Will record unemployment and poverty figures still be on the headlines? Or will we meet instead to report on a strengthened and more reliable global economy, falling CO2 emissions and significant progress in achieving the Millennium Development Goals (MDGs)? Our policies and decisions today, and the coordination amongst them, will determine our future.

The solutions for a crisis, drafted in the midst of the urgent, often create the conditions for the next one. A quick example is the way in which the current restoration of the financial system and economic growth is causing unprecedented pressure on public finances, producing public deficits and debts that will linger and limit the scope for public policy for decades.

We are standing at a foundational moment. This is not only the greatest crisis of our lives; it is also the greatest opportunity, and the greatest responsibility of our lives. Let's not waste this crisis. Let's prove Carlos Fuentes right and produce together, through enhanced multilateral cooperation, that improved offspring which will surpass this crisis and redeem it. Let's create a better world economy founded on new values and greater trust. Let's be optimistic. At OECD, like Sylvia Ostry, we believe this new better world is achievable. For it might very well be true, in the words of another famous North American, Leonard Cohen, that: "even damnation is poisoned with rainbows".

Thank you very much.

ⁱ In the words of Yann Arthus-Bertrand.

ⁱⁱ ILO, “ILO says job losses are increasing due to economic crisis”, Press release 28 May 2009. See: http://www.ilo.org/global/About_the_ILO/Media_and_public_information/Press_releases/lang--en/WCMS_106525/index.htm

ⁱⁱⁱ Tom Keating, “Multilateralism and Canadian Foreign Policy: A Reassessment”, Canadian Defence and Foreign Affairs Institute, p.1