OPINION:

A small country voice for the G20

David Skilling & Michael O'Sullivan

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A small economy perspective can contribute distinctive insight to G20 policy debates

As G20 Finance Ministers and central bankers meet in Shanghai today, there will be much to discuss. The global growth outlook is soft, with significant downside risks, even if a full-blown growth recession remains unlikely.

Uncertainty about the economic outlook is reflected in financial sector turbulence. The recent equity market sell-off has pushed many risk and market stress indicators to levels not seen since 2009 and 2011. And credit, profit and interest rate cycles, which historically tend to move together, are also out of kilter.

Alongside these current issues, the post-crisis global economy is characterised by slowing international trade and weak productivity growth. Many of the traditional policy instruments are increasingly ineffective in dealing with these structural issues. New policy responses are required to strengthen medium-term growth potential.

To justify its labelling as the world's premier economic forum, the G20 need to take a lead on clear communication of these challenges, as well as the short and medium-term policy responses that are required. Given China's increasingly central place in the global economy, the chairing of the G20 by China is timely. It is an opportunity for China – and for the other major economies – to restore confidence and stability in the global economy.

Although the G20 is a grouping of the world's large economies, we believe that small advanced economies can make a substantive contribution, offering distinctive insights on these issues. We identify three specific insights from small advanced economies.

First, small economies provide important calibration on the weak state of the global economy, clearly identifying an urgent need for active policy action that is not particularly evident across the large economy G20 group. G20 economies would do well to consider what is happening in small, developed countries – the canaries in the coalmine of the global economy.

Small, developed economies are highly open to the global economy, performing strongly over the past decades in a period of intense globalisation and strong global growth. But despite strong policy settings and agility, many of these small economies are telling a similar story: markedly lower post-crisis GDP growth rates, a much weaker export engine, and the adverse impact of disruptive cross-border capital flows.

The reduction in small economy growth rates since the crisis has been bigger than for larger economies. And the quarterly GDP growth of 15 small advanced economies softened further in the second half of 2015, converging to large economy growth rates. After a sustained period of over-performance, small open economy growth is slowing – reflecting a structurally weaker global economy. Small economies do not provide signs that a recovery is imminent.

Second, small economies provide useful policy insights on responding to a weak global economy. In last week's OECD Economic Outlook, in which the global growth forecast was marked down, there was a call for collective, coordinated policy action on a range of fronts. Small economy 'laboratories' have useful perspectives on how to approach this in areas like monetary policy. While Japan has recently discovered the limitations of negative interest rates, small economies like Sweden, Denmark and Switzerland have been grappling with this for some time.

Moreover, small economies in Europe and Asia have been amongst the first to feel the negative consequences of quantitative easing in the larger economic regions and, in this way, to signal that new departures in monetary policy have limitations. Small economies are also in the forefront of disruptive cross-border capital flows, partly due to a lack of international policy coordination. This small economy experience suggests that greater coordination is needed for measures to stimulate global demand to be effective.

Small economies also suggest that global stimulus efforts should be rebalanced towards intelligent fiscal activism. This could be directed to address infrastructure deficits, as well as investing in education and innovation, in both developed and emerging countries. Small economies take fiscal discipline seriously, but fiscal policy offers more potential than further monetary loosening.

Third, small economies can offer distinctive perspectives on responding to the structural changes underway in the global economy – new technologies, business models, and markets. These are having a profound effect already on growth, productivity, labour markets and the income distribution.

Policy issues with respect to education, innovation, infrastructure, tax and social insurance systems, will become increasingly prominent. Because of their acute exposure to global economic dynamics, small economies are already in the vanguard of policy innovation on these and other issues.

Similarly, small economies have distinctive insights on how best to approach a new settlement on the nature of globalisation: from the design of regional and bilateral trade agreements, to the management of global capital flows and exchange rates.

Overall, small economies are well-positioned to contribute insight to the policy issues on the G20's agenda in 2016. The G20 countries may make the world go around, but large economies do not have a monopoly on wisdom. The G20 should be listening to the voice of small economies that are deeply exposed to changes in the global economy, and have distinctive perspectives on how best to respond to these global dynamics.

About the authors

Dr David Skilling is the founding Director of Landfall Strategy Group, which was established in 2011. David advises governments, companies, and financial institutions in several small countries, and writes regularly on global macro, globalisation and geopolitics from a small country perspective. David has recently served as Senior Advisor to the Secretary of Foreign Affairs & Trade in New Zealand, and as a Fellow at Singapore's Civil Service College. Previously, David was an Associate Principal with McKinsey & Company in Singapore, as well as being a Senior Fellow with the McKinsey Global Institute. Before joining McKinsey, David was the founding Chief Executive of the New Zealand Institute, a privately-funded, non-partisan think-tank. Until 2003, David was a Principal Advisor at the New Zealand Treasury. David has a Ph.D. in Public Policy, and a Master in Public Policy degree, from Harvard University, as well as a Master of Commerce degree in Economics from the University of Auckland.

Dr Michael O'Sullivan is a Managing Director of Credit Suisse in the Wealth Management Division, based in Zurich. He is Chief Investment Officer for the International Wealth Management Division. He joined Credit Suisse in July 2007 from State Street Global Markets. Prior to joining Credit Suisse Michael spent over ten years as a global strategist at a number of sell-side institutions and has also taught finance at Princeton and Oxford Universities. He was educated at University College Cork in Ireland and Balliol College in Oxford, where he obtained M.Phil and D.Phil degrees as a Rhodes Scholar. He is an independent member of Ireland's National Economic Social Council. He is the author of two books, including 'Ireland and the Global Question'.