The Economic Agenda of the French Presidency of the G20: Context and Challenges

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French diplomacy had long pinned its hopes on the G8 presidency that was to return in 2011. Even before the financial crisis, internal discussions had been initiated on what was then already obvious: the rise of emerging countries strongly limited the representativeness of the G8, the group of heads of state and government, which was established in 1975 to discuss world affairs. The original idea was to expand the G8 to include five or six emerging countries' representatives in order to improve the economic and geographic representation. The financial crisis has precipitated, but also thwarted this plan.

Including large emerging countries in order to seek cooperative solutions to overcome the financial crisis, then at its height, was indeed the main purpose of the meeting between Nicolas Sarkozy and George W. Bush at Camp David, October 19, 2008. However, it was the White House that decided the final format of the summit in Washington, November 8, 2008. Thus, all the heads of state and government of the "G20", the group that was brought together, since 1999, of finance ministers and central bank governors of the G7, including 11 emerging countries[1], Australia and the European Commission, were invited to attend. In addition, the Netherlands and Spain, while not being official members of the G20, were allowed to attend the meetings. It is in this configuration that the summit of Washington took place and also the four summits that followed: London (April 2009), Pittsburgh (September 2009), Toronto (June 2010) and Seoul (November 2010). It was agreed in Pittsburgh that the pace of summits in 2011 would be annual and that France would exercise a dual presidency in 2011, the G8, long anticipated, and the G20. In 2012, Mexico will chair the G20 and the United States the G8.

The short history of the G20 summit is divided into two phases. Washington and London took place at the peak of the 2008-2009 crisis. In November 2008, as the financial markets were collapsing, the Washington summit gave its participants the opportunity to express its willingness to cooperate, to detail an agenda and to assert that the use of protectionism would not be a solution to the crisis. The conclusions of the London Summit in April 2009 developed more specific guidance: fiscal support to the economies was

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[1] China, India , Russia, Korea, Indonesia, Mexico, Argentina, Brazil, South Africa, Turkey, Saudi Arabia.

endorsed and cooperation for a better regulation of international finance took shape. From the Pittsburgh summit (September 2009) on, the G20 had moved from a crisis management mode to a steering committee mode. Since decisions are made by consensus, each country became less willing to make concessions. The work has been laborious and results have been limited. The Canadian presidency (Toronto, June 2010) was disappointing. The reliability and quality of the preparation of the Seoul summit (October 2010) by the Korean Presidency had certainly been welcomed, but the results were modest.

If absent of the current sovereign debt crisis in the Eurozone, the challenge of the Cannes summit for the French authorities would have been to ensure that visible progress is made on the topics which the G20 has been working on for three years (global imbalances and financial regulation) and the priorities it had decided to include (the reform of the international monetary system and stabilization of commodity prices and oil). The Eurozone crisis and other possible developments might very well hijack the summit, which would then return to the crisis management mode.

Building on the legacy of the first summits

France has inherited two major issues from the previous summits: financial regulation and the rebalancing of the world economy through the coordination of macroeconomic policies.

1.1 The regulation of global finance

The crisis highlighted many flaws in the financial sphere. Their accumulation has led to the formation of pockets of excessive risks that eventually busted and shook the financial system as a whole.

Among those flaws, one can mention at the level of financial intermediaries: faulty risk analysis, over-reliance on ratings, compensation policies that encourage risk taking, the multiplication of layers of financial intermediation, excessive complexity of financial products, excessive asymmetry between the maturity of resources and assets, insufficient loss-absorbing capital buffers and, as a consequence, too much debt.

The crisis also highlighted shortcomings in the institutional design of financial regulation and in the institutions in charge: limited scope of regulators' jurisdiction, overlapping between jurisdictions, complex borders and flawed performances for varying reasons: inadequate human and material resources, conflict and competition among regulators, lack of coordination at the national or international levels, lack of willingness to effectively exercise the powers they have, inapplicability of certain rules and finally, lack of global perspective on risk.

The mechanisms for managing systemic risk (i.e., the role of lender of last resort of national central banks, funds guaranteed domestic bank deposits and treasuries' interventions) generally worked well. But it became clear that their mere existence encouraged risk taking and the way they worked led to an excessive cost transfer to the taxpayers and society as a whole, be it direct (rescue of financial intermediaries) or indirect (cost of recessions resulting from financial crises).

Overcoming these deficiencies and shortcomings in an overall reform of financial regulation is a very difficult task. First, uncertainty and complexity are inherent to finance. Second, levels of regulation before the crisis were very numerous, fragmented between different levels of government (sub-federal, state, international) and between different types of activities (insurance, financial markets and banks). Third, the legal traditions differ from one region to the other. Fourth, the lobbies in this sector are particularly strong. Finally, the solutions for the most part remain to be invented. They are necessarily complex to design (for example, imagine mechanisms for managing cross-border institution failures), to implement (for example, in tax heavens) and to control (for example, compensations in the financial sector). This inevitably leads to a trial and error process that is difficult to explain to public opinion. Moreover, as far as its financial dimension is concerned, the crisis hit emerging markets only marginally. While it was in their best interests as suppliers, creditors and debtors of industrialized countries that the latter do not fall into depression, they felt relatively little concerned with the purely financial dimension of the crisis. They were also reluctant to impose solutions that could penalize their own financial industry in the future. Industrialized countries themselves were affected unevenly by the financial crisis. The Canadian financial system, for example, remained remarkably resilient.

Given the limitations inherent to the issue of financial regulation and the institutional nature of the G20, one can draw a rather positive assessment of the initial political impetus given by the Summits of Washington, London and Pittsburgh. An important element was to strengthen the role of coordination and control of the Financial Stability Board (FSB), deriving from the Financial Stability Forum (FSF), established in 1999 along with the G20 Finance. The Pittsburgh Summit (September 2009) launched the reform of banks capital and liquidity ratios (the so called "Basel 3 agreement"). Many initiatives were launched in other international fora of national regulators that are members of the FSB: the International Association of Insurance Supervisors (IAIS), the International Organization of Securities Commissions (IOSCO) and the International Accounting Standards Board (IASB).

However, the political dimension of the G20 led to focus on certain ideas, sometimes to the detriment of a comprehensive approach. For example, the French president chose to focus on the issue of compensation; the US Treasury Secretary emphasized the need to increase bank capital.

From the Pittsburgh summit on, the G20 experiences difficulties in dealing with financial regulation and communicating its actions. Press releases from

Toronto and Seoul mentioned the topic at length, but by listing the projects in progress. This does not give a real sense of political leadership.

Moving out of this technical and compartmentalized approach will be all the more difficult for France as the sense of emergency on financial regulation has somewhat vanished. This would require identifying themes that are both mobilizing and uniting.

The regulation of global finance: An inventory of ongoing projects

Created after the Asian crisis at the same time as the G20, the Financial Stability Forum (FSF) was transformed into the Financial Stability Board (FSB) at the London summit (April 2009). It is composed of representatives of finance ministries, central banks and financial regulatory authorities of the G20 countries, as well as Hong Kong and Singapore. Relevant international organizations in the field of regulation are also represented. The G20 de facto delegated to FSB the task to coordinate the many initiatives that took place after the crisis in the field of financial regulation. In its latest report on the implementation of the recommendations of the G20, FSB summarizes the ongoing projects without prioritizing them. This list provides an overview of the wide variety of topics:

- Capitalization and liquidity standards for banks (Basel 3)
- Specific risks posed by systemic institutions
- Special rules imposed on global systemic institutions
- Bankruptcy (resolution) of cross-border systemic institutions
- Quality standards to be met by national regulators
- Supervision of the "shadow banking" (de facto financial intermediaries playing the role of banks but not subject to banking supervision).
- The functioning of organized and over the counter derivatives markets for raw materials or
- The development of "macro-prudential" regulatory framework
- The convergence towards more stringent accounting standards
- The monitoring of the implementation of international supervision and control standards (peer review, reforms of compensation, exchange of information, coding standards)
- Consumer protection in financial services
- Reducing the reliance on rating agencies
- Data sharing on the interconnection between the institutions and the systemic risks they face
- The ethics of market participants

1.2 Focus the debate on 'global imbalances' on structural issues

By proposing the adoption at the Pittsburgh summit of a "Framework for a strong, balanced and sustainable growth", the United States echoed the debate between them and China since the 2000s on the latter's exchange rate policy. They feel that this policy led to undervaluation of the Chinese currency and has given Chinese exporters an unfair competitive advantage.

The mainly fixed exchange rate policy conducted by China, together with the prohibition of overseas investment for Chinese residents, has in fact contributed to the unprecedented accumulation of foreign reserves by the country since the late 90s. This accumulation has ultimately helped to finance the US current account deficit that widened until 2007, then reduced during the crisis and now increasing again.

In 2006-2007, the debate on global imbalances has acquired a second component. The accumulation of surpluses in oil and commodities producing countries, due to the sharp increase in prices, led to a rise of sovereign wealth funds entrusted to reinvest some of that surplus. The contribution of these funds to recapitalize the US financial sector in early 2008, after the first phase of the crisis, however, quickly helped to put this issue into the background and the debate has therefore focused only on the Chinese exchange rate policy.

The initiative of the US administration to Pittsburgh was probably aiming at several objectives. The first was to respond to the pressure that Congress had exercised over the executive for many years. Indeed, Congress regularly threatened to vote against one of the many bills before it in order to punish China for its currency policy. The second objective was to get out of the direct confrontation with China by raising the issue of trade surpluses as part of a forum involving other countries with structural surpluses such as Japan and Germany. The third objective was for China to face its responsibilities in an environment where it might be more accountable for its decisions than in the one of the US-China direct bilateral talks, in particular the strategic dialogue begun in 2006 by the Bush administration and continued in a modified form by the Obama administration.

Although China and the United States are not—by far—the only players in the debate on global imbalances, this debate is indeed one of the many dimensions of the strategy that takes place face to face between the two countries. Each places the responsibility for creating these imbalances to the other, the US stressing the savings glut in emerging markets and China the excess of debt in the United States.

In fact, both countries are confronted with exactly symmetrical problems that neither one nor the other can overcome. On the American side, the savings are insufficient to support a level of investment necessary for growth. The crisis resulted in an increase in household savings and a collapse in private investment. That helped to reduce the imbalance between savings and investment, despite the widening budget deficit. However, the structural factors responsible for this imbalance have not been addressed: the excess of domestic demand, especially consumption, while household debt is promoted by the tax code and stimulated by the financial sector for which it represents a lucrative line of business. The choice of the US authorities in 2008 and 2010 to do everything they could to prevent an economic depression by stimulating demand, while certainly justified in the short term, resulted in more debt for the federal government. In this respect, it has only slowed down the adjustment.

On the Chinese side, the authorities which have, so far, had a remarkable mastering on domestic economic developments, are now facing difficulties in implementing reforms.

Thus, for many years now, the Chinese authorities have expressed their wish to reduce the excess of domestic savings by boosting domestic demand and, in particular, household consumption (about 40% of GDP less than investment) at the expense of business investment and the export sector.

Reaching this goal requires (i) to reduce the incentives to save through the development of transfers of income (through pensions, sick leaves…); (ii) that household income grows faster than the economy; and (iii) to better reward the existing savings and make savings allocation more efficient, including avoiding over-investment in the export sector or in some speculative areas of the domestic economy.

The real wages in China have indeed increased and the collective financing of education and health is in progress. However, the authorities are very reluctant to take steps that could have a negative impact on the export sector or that could limit access to cheap financing for state-owned enterprises and local communities. Such measures would focus on the gradual liberalization (and control) of the domestic financial sector, removing most of the advantages enjoyed by Chinese exporters and the nominal appreciation of the RMB would increase the purchasing power of Chinese overseas. Then, the issue of nominal exchange rate of RMB is nothing but a piece of a puzzle.

The difficulties the Chinese authorities are facing can probably be explained by two factors. On the one hand, they fear social unrest that could result from a policy of industrial and financial restructuring. On the other hand, they face a powerful coalition of interests that they have no capacity or political will to counter, especially in a transition period at the helm of power. This coalition brings together (i) local authorities that enjoy easy access to credit from the Chinese public banking sector and also benefit from the housing bubble which increases the value of their assets; (ii) state-owned enterprises, often linked to previous and like them deriving significant benefits of the current situation: cheap financing, rapid increases in asset prices and support for China's exports; and (iii) banks who fear the impact on margins of the financial sector liberalization.

Therefore, the world rebalancing of the economy is now largely in a dead end. A deep financial crisis in the United States did not lead to a sustainable reversal in trend. The occurrence of a crisis in China cannot be excluded. It could take the form of the bursting of the housing bubble or chain defaults on the part of local borrowers. It would probably lead to measures to stimulate domestic demand and a recapitalization of the financial sector. Like in the US, the aim would be to avoid a depressive spiral, but this would limit the room for maneuver and future government, also it could have social and political consequences beyond the control of the local authorities.

Therefore, action to prevent further deterioration of global imbalances and, if possible, remedy are needed. Can the G20 contribute?

In theory, a consultation of all stakeholders in the global economy, each taking into account the constraints of others, is likely to lead to a better result than the result of isolated decisions. France is traditionally very supportive of this approach.

In practice, the use of the G20 by the United States as a mostly media-oriented opportunity (this is to show the public and Congress that the executive branch is active in addressing the RMB overvaluation issue) has adverse effects. Of course, a trade war between the two countries—that's what some members of Congress have been proposing for six years—would have more disastrous consequences. But the American approach, which originally was intended to broaden the dialogue on global imbalances, results in a dramatic questioning over the exchange rate policy in China. The latter is detrimental to the rest of the world and, probably today, to China itself. However, most recent studies suggest that, as is usually the case, even a stronger nominal appreciation of RMB would have a limited impact on the Chinese trade balance and more on the balance between bilateral US and China trade.

In addition, as shown in the above analysis, the problem is much broader than just China's exchange rate policy. Any solution can only result from structural measures implemented by both sides. These measures, namely the stimulation of consumer demand in China and reducing the bias of the American economy in favor of debt, would only marginally contribute to reducing the global demand for raw materials and hydrocarbons. Therefore, any policy aiming at reducing global imbalances should include steps to reduce per capita energy consumption, particularly in the United States and Canada, where it is highest. On this point, the G20 action was limited to promote the elimination of oil subsidies in developing countries. While these subsidies have distorting effects, the impact of their removal on global demand for oil will likely remain low.

In addition, the G20 could have a positive impact on global imbalances if an agreement is reached to focus on long-term issues; that is, if the meetings are not hijacked by short-term considerations, which is difficult considering the high level and the political responsibilities of summit participants. In any case, the consensual and non-binding nature of the G20 will necessarily limit the scope of its practical resolutions.

The international discussions on global imbalances

In 2006-2007, the first round of "multilateral consultations" on global imbalances is engaged at the IMF. The crisis quickly puts an end to it.

A US initiative at the Summit in Pittsburgh leads to the adoption of a "Framework for a balanced and sustainable growth". This framework consists mostly of a peer review (mutual assessment process - MAP) that aims at monitoring the consistency between national economic policies and "common objectives". The IMF provides technical support.

At the summit of Toronto, the IMF presents a scenario of economic cooperation asserting that this scenario would lead to an outcome that would be more favorable than the one resulting from the simple aggregation of information transmitted by the G20 members on their economic policies and their own forecasts.

In Seoul, in November 2010, discussions focus on the evaluation criteria of the economic policies followed by G20 members. The US proposal to collectively determine targets for the current account of balance of payments is denied. However, it is agreed that a list of "systemic countries" would be compiled and a report on the impact of external economic policies of each would be drafted by the IMF ("spillover reports") on the basis of a set of indicators previously defined collectively.

Meetings of finance ministers and central bank governors of the G20 countries in February 2011 in Paris, and in April 2011 in Washington, focus on identifying systemic countries (China, India, France, UK, Germany, USA, Japan) and "guidelines" for the selection of indicators. It appears that the IMF has decided to join "Spillover" and "Article IV consultation" reports (Article IV reports are the ones that the IMF writes, generally each year, on the economic situation of each member state). Hence spillover/article IV consultation reports are released, the IMF on the US and UK in July 2011. A meeting of G20 finance ministers in Paris in October 2011 should lead to a set of "recommendations" aimed at the Heads of State and Government. These recommendations would result from the analysis of the spillover reports.

2. Achieve concrete results on the priorities set by the Presidency

In addition to financial regulation and global imbalances, the French Presidency intends to engage a discussion on two other factors of financial instability: the reform of the international monetary system and the volatility of commodity prices.

2.1 Diminished ambition on the reform of the international monetary system (IMS)

The Bretton Woods agreement in 1944 sanctioned the monetary hegemony of the US dollar. Parity between the US dollar and the currencies of countries that signed it was fixed (possibly adjustable in case of "fundamental disequilibrium") and the United States ensured that their central banks could exchange their dollar reserves into gold. The International Monetary Fund (IMF) was to assist countries facing external imbalances, enabling them to undermine the parity of their currencies with the dollar. These agreements put an end to 25 years of major monetary turbulences that the industrialized world had known after the First World War.

However, the dollar hegemony was quickly challenged. The recovery of European countries' export capacities and the recurrent deficit of the balance of payments of the United States flushed the international financial system with dollars, which led to a trend depreciation of the dollar.

In the sixties, France challenged the "exorbitant privilege" (the expression was coined by Valery Giscard d'Estaing, then French Minister of Finance) enjoyed by the US as the international monetary system allowed it to finance almost indefinitely its external deficits by issuing its own currency. Furthermore, this ability was not affected by the abandonment of the US dollar's convertibility into gold at fixed rates in 1971, the subsequent introduction of floating exchange rate regimes and the successive efforts of Europeans to stabilize fluctuations between the parities of their respective currencies ("European currency snake" and "European Monetary System") or the creation of the Euro.

Revived in the late seventies after a decade of inflation and as the US economy seemed permanently weakened, the debate over the international monetary system has had a long sluggishness since then. Despite the many financial crises, it was not until the crisis of the late 2000s that this debate modestly resurfaced.

During the 2000s, the United States accumulated deficits and foreign debts and, symmetrically, the foreign exchange reserves of emerging countries have sky-rocketed. During the financial crisis, direct arrangements between central banks made it possible for non-US banks to meet the sudden increase in demand for dollar.

It is in this economic and financial environment and in the middle of the financial crisis that the debate over the IMS was revived. The most spectacular initiative came in March 2009 from a short paper written by Zhou Xiaochuan, the governor of the PBOC (People's Bank of China PBOC).

On a technical level, this debate has four components (besides the one on the coordination of economic policies addressed in the development on global imbalances (see above):

1. Will the dollar retain its hegemonic position? This position of dominance exists for trade invoicing, and international financial transactions and reserve assets. Historically, gold and sterling had also played this role. The Deutsche mark, French franc and the euro, the yen or the Swiss franc also played an international role, though much more limited. A central question of reform of the IMS is whether the dollar will keep, share or lose this dominant status and what are the advantages and disadvantages of

the emergence of competing international currencies such as the Chinese renminbi or the euro.

2. What is the role for the IMF? The International Monetary Fund (IMF) was created by the Bretton Woods agreements as the central institution of the international financial system. In practice, it has been important—and controversial—in the management of financial crises. It has, however, remained a marginal actor of the international monetary system. In the late sixties, it was nevertheless decided to create a specific currency unit for the IMF, the Special Drawing Rights (SDRs), whose value changes according to a basket of currencies. But this has not led the IMF to play an active role in financial intermediation among its members. In particular, claims on the Fund or other debtors denominated in SDRs have not become an important reserves instrument for central banks.

3. How to stop the accumulation of foreign reserves? Since the late 90s, the overall level of exchange reserves has strongly increased, outpacing nominal GDPs. A decisive factor in this increase was the humiliation felt by Asian countries after the IMF interventions resulting from the crisis in the region in 1997 and 1998. These have drawn the conclusion that only a very high level of reserves was likely to protect their currencies against speculative attacks. The accumulation of foreign reserves also results from the overall role played by US financial institutions, which gives an incentive to accumulate dollars, and "global imbalances" (see above). The level reached by the foreign exchange reserves has become excessive; it helps to maintain the deficit and diverts capital from emerging markets of more productive employment than say, funding US consumption.

4. Do we need international guidelines or rules for the international flows of capital? Most industrialized countries severely restricted the free movement of capital between residents and the rest of the world after the Second World War. These restrictions were completely lifted in the late 80s. In the 90s, the IMF strongly encouraged the emerging and developing countries to remove them completely, including restrictions on short-term capital flows. This policy was highly controversial and the IMF itself has begun a self-examination about it. The debate was revived by the restrictive measures taken by several emerging countries at the end of the financial crisis and then in the fall of 2010. Dissatisfied with the appreciation of the Brazilian currency resulting from hot money inflows, partly due to a very accommodative US monetary policy, the Brazilian Minister of Finance spoke of "currencies war".

The French authorities have taken on their own revival of the debate during the preparation of their presidency of the G20. They insist that IMS reform would contribute to substantially reducing the volatility of exchange rates and the likelihood of financial crises. In addition, they may have been sensitive to the Gaullist tone of the project. A reform of the international monetary system could only lead to mitigating the influence of the dollar and that of American finance in the world. A greater role would be entrusted to the IMF, an international financial institution that has often been led by a French citizen. A future arrangement could also benefit the development of the international role of the Euro, if it manages to overcome the current crisis.

Since launching this idea, the French authorities have lowered their goals. They have repeatedly stated since the beginning of 2011 that their objective is not to address the dollar or to return to a fixed exchange rate system. The immediate results of this initiative will certainly be modest. The debate now focuses on two points:

- The inclusion of the RMB or other emerging currencies in the "currency basket" from which the daily value of the DTS is calculated. This inclusion would be perceived by China as a step towards the creation of alternative international reserve assets to the dollar. The statement issued after the meeting of G20 finance ministers in April on the subject, indicates that the enlargement of the basket of currencies used to calculate the value of the SDR will be "based on criteria," with no additional detail. This suggests that the developed countries are willing to put preconditions on the inclusion of the renminbi in the DTS basket.
- Working out a code of conduct to guide the use of restrictive measures of capital flows. The underlying idea is to limit the use of these measures to the case where the hot money inflows threaten the financial stability of a country while the economic policy of the latter is not excessively procyclical. It is also to promote fiscal measures rather than quantitative restrictions. The possibility of giving the Fund jurisdiction over capital flows—which is not the case at present—is also discussed. In both cases, it is unlikely that emerging countries will accept binding patterns.

The final statement could also include references to the accumulation of foreign exchange reserves and measures to limit them (develop local financial markets, making it easier to access IMF financing, promoting the idea of pooling some of the reserves through the concept of "safety net"), but probably these references would be more of a ritual than a result in further concrete action.

Despite the modesty of its predictable outcome, the French initiative has the advantage of starting—indirectly and perhaps unintentionally—the international debate on the monetary consequences of the transformation of China into a major economic power. This is probably the major issue for international monetary relations in the next two decades. Until now, these consequences have been limited. China has accumulated $3000 billion in foreign reserve. Its banks have accelerated their international development. Its sovereign wealth fund, CIC, invested in foreign financial institutions, including American ones. Exchange rate policy and fiscal policy in the countries of East Asia and Southeast Asia are increasingly determined by the choice of China. But the RMB is not convertible. Most of the monetary relations between China and the world continue to be made in dollars, which exposes the Chinese companies and banks to currency risk and interest rate differentials. With the crisis, the Chinese authorities, however, have embarked on a deliberate policy of internationalization of the RMB through the financial center of Hong Kong. 10% of deposits in banks are already denominated in RMB and invested either in bonds issued in RMB in Hong Kong (dim sum bonds) or in the interbank market in China. This policy, however, will stay limited if the strict measures of capital controls (i.e., non-convertibility of the RMB) are maintained.

Toward a multipolar international monetary system?

Some authors consider a world in which two or three currencies (the dollar, the Chinese RMB, and if the ongoing crisis is overcome, the Euro) would have the status of "international currency", that is to say, a currency which is used for transaction purpose in trade, storage of value for other states (foreign reserves) and anchor currency for exchange rate policies in countries within their area of monetary influence.

This is especially true for the American economist specializing in international monetary system, Barry Eichengreen, and authors of the recent report *Global Currencies for Tomorrow : A European Perspective* (2011). The latter examines in detail the conditions for a rise of the Chinese currency. The authors observe that the acquisition of international currency status is based on several criteria: economic power, political power and the will to exercise global leadership, domestic financial sector development and the quality of governance of the domestic economic and financial institutions, and, finally, the evolution of monetary systems and exchange rate policies.

2.2. Mobilizing on the stabilization of commodity markets

In the second half of 2000, there has been a simultaneous increase in the level and volatility of commodity prices and oil prices. The range of motion and the fact that they occurred for a number of products in a period of time before and after the financial crisis, have triggered feelings that these prices could be manipulated and that public intervention might be needed to "stabilize" or even reduce them. Due to the fact that commodity markets are global, the subject seemed to the French authorities to be an ideal candidate for the agenda of its presidency of the G20.

Recent developments in the prices of raw materials and hydrocarbons can be partly explained by conventional market analysis tools. The rapid growth in demand from emerging markets has pushed up prices for products whose marginal cost of production increases. In addition, commodity prices evolve in a nonlinear way and are therefore volatile, because of the role played by inventory levels in the price discovery mechanism. A decline in inventory levels below a threshold seen as critical by the market led to a sharp increase in prices, and vice versa. It is possible that a rapid change in quantitative and geographic demand and uncertainty about the economy have contributed to make it more difficult to anticipate demand and, consequently, increased the volatility of inventory levels and prices.

It is likely that we should add one additional explanation for increased volatility, which lies in the growing role played by financial investors in these markets. Inventories of raw materials were traditionally considered as companies' current assets. They now tend to become assets on which financial investors take positions, be it on the physical markets or, more commonly, on the derivatives markets. The low interest rates reduce the opportunity cost of holding these assets and encourage investment. The ability of fund managers of major American universities like Harvard or Yale to anticipate this trend had yielded outstanding results in the mid-2000s. This approach is now shared by many types of investors: pension funds, hedge funds, investment banks, specialized subsidiary created by producers or traders of raw materials. Investors look to invest in products where they feel the price does not reflect the balance between supply and demand. But in doing so, they counteract or amplify current developments and, ultimately, the volatility. They are active on the physical market, but also on the future markets, which have developed significantly and whose price movements can have consequences down on the spot markets.

In addition to these structural transformations, one must also consider identified or suspected market failures. The opaqueness of these markets is often criticized. The concentration of the actors, especially on the supply side, is likely to facilitate agreements or abuse of dominant position. As for financial markets, a share of transactions takes place outside any regulation. Finally, in response to the volatility and price increases, several countries (like China and India) have taken measures to restrict the export of their agricultural products. These measures have led to isolation of the local market from the world market and brought prices down, reducing the incomes of local producers, but increasing the purchasing power of consumers and contributing to an increase in the world price.

This complex situation legitimizes that public authorities and citizens be better informed. It justifies that actions be taken to compel the operators to provide the information needed to assess the situation, while respecting the confidentiality of their business operations. The detailed analysis of this information may reveal regulatory requirements, particularly with regard to fair competition, risk management in particular.

The idea of direct intervention of public authorities in the markets to influence prices is of a different nature. Such interventions, if they are agreed, would involve the mobilization of significant financial and technical capacities, generating long-term fixed costs. They would also require the building up of institutions that have knowledge of the equilibrium price of each product and have the means to force the participants to achieve this price. Such a project echoes the funds used in the seventies to stabilize the export earnings of developing countries (Stabex Sysmin etc.). Should it be proposed by a summit participant, the response to such a solution would most likely be rejected.

Moreover, despite a political tone that could evoke the idea of direct intervention in the markets, the agenda of the French Presidency in this area seems to finally focus on agricultural markets and on the transparency and regulation issues (actually financial regulation rather than antitrust regulation).

For the first time France has organized a special session of the G20 at the level of agriculture ministers on June 22 and 23, 2011 in Paris. They have agreed to submit to heads of government and state gathered in Cannes a "Plan of Action on the volatility of food prices and agriculture" in five areas (see box) and to launch the "Information System on Agricultural Markets"(Agricultural Market Information System-AMIS). This information system is designed to encourage the main actors in food markets to share their data, improve existing information systems, promote a better shared understanding of the evolution of food prices, and promote political dialogue and cooperation. AMIS will be hosted by the Food and Agriculture Organization.

The five goals of the "Action Plan on the volatility of food prices and agriculture" are inspired by a joint report produced by nine international organizations that was commissioned by the participants at the Seoul Summit:

(i) improving production and productivity in agriculture in the short and long term to meet a growing demand for agricultural raw materials;

(ii) strengthening information and market transparency to give a more solid basis for expectations of governments and economic operators;

(iii) strengthen policy coordination to enhance international confidence in international markets and prevent crises and food markets and respond more effectively;

(iv) improve and develop the tools of risk management for governments, businesses and farmers to enhance their ability to manage and mitigate risks associated with the volatility of agricultural prices, particularly in the poorest countries;

(v) improving the functioning of commodity derivatives markets.

The "financial regulation" dimension of the stabilization of commodity markets, especially derivatives markets, however, remains the responsibility of the finance ministers and central bank governors. It is said that a special session of the G20 finance should be dedicated to this topic. At their meeting in Washington on 14 and 15 April 2011, the ministers and governors stressed the need that market participants in derivatives commodity markets be subject to "appropriate" regulation and supervision and called for greater transparency in spot and derivative markets. They delegated to the International Organization of Securities Commissions (IOSCO) the responsibility to decide on the "recommendations" that national authority should follow in this field and wished that they dealt with "among other subjects" position limits in order to fight price manipulations and market abuses.

Finally, a report on the relationship between agricultural policies in developing countries and the volatility of commodity prices was commissioned to the French economist Pierre Jacquet. An interim version entitled "Improving risk-management to better cope with food price volatility: How can the G20 help Developing Countries?" was released on May 15, 2011. This report underlines that if the volatility of domestic agricultural prices is linked to international prices, transmission in the domestic markets of the volatility depends on many factors specific to each country (exchange rate policy, transport costs, regulations etc.). Any hedging strategy is therefore country-specific. The report recommends that the G20 focuses on large-scale shocks on prices that have high costs for the poorest countries and on the volatility of prices paid to producers. It stresses that direct interventions on prices are not sustainable. However, global agricultural policies are needed. These policies should focus on the *ex ante* risk management in developing countries, particularly through training programs on the use of hedging instruments and the introduction of intermediaries to facilitate access to these instruments. The report also suggests that emergency responses to food crises should be improved through a better management of emergency inventories and recommends that donors should explore the possibility to sign "smart contracts" with producers that protect the latter from part of the price risk.

Beyond the substance, the major international summits are very tricky arenas for communication. The previous summits have shown that the last news could prevail on issues debated at length. In the case of Cannes, it is likely that the sovereign debt crisis in the Eurozone will draw a great deal of the attention, even if not officially on the summit agenda. Some countries may also want to attract attention to their ideas by circulating their proposals at the last minute, which can undermine the agenda of the presidency. The United States played this game in the past. They put forward their proposals on banks' capitalization and on global imbalances a few days before the Pittsburgh summit in September 2009. They voiced their idea of numerical targets for current accounts the same way before Seoul in 2010. The debate on global imbalances is also dependent on the cyclical state of relations between China and the United States and the communication strategy of the US authorities vis-à-vis the US public opinion and the US Congress. The strong emphasis that is therefore put on the Chinese exchange rate policy to the detriment of other structural factors behind these imbalances crystallizes the opposition and ultimately leads to an opposite effect to the one that was intended.

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