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ICC Regional CEO Forum 21-22 November Hong Kong Executive Summary

Introduction

On 21-22 November 2008 in Hong Kong, ICC convened a forum of more than 150 CEOs and senior executives from major corporations in the Asia-Pacific region as well as ICC Executive Board members from across the world, to exchange views on the challenges facing the global economy and to propose solutions.

In his welcoming address, **Victor K. Fung**, Chairman of ICC, dispelled the notion that the 21st century would be the “Asian century”. It is, and will remain, the “global century” with global issues calling for global solutions. In this global century, Asia will be expected to play an increasingly influential role as a major emerging force in global trade and investment.

An immediate focus of the forum was to identify responses for limiting the damage caused by the current financial crisis. The forum also explored longer-term approaches for reconstructing the global economic system. The following is an account of two days of interactive discussions, covering issues of trade, finance, climate change and the role of Asia in today’s interdependent world economy.

Plenary session 1

The first plenary session of this conference was addressed by **Supachai Panitchpakdi**, Secretary-General of the United Nations Conference on Trade and Development (UNCTAD) and former Director-General of the World Trade Organization (WTO), who offered his perspective on the financial crisis and its implications for Asia.

The crisis has come after a long period of buoyancy and global economic expansion, largely led by rapid growth in the developing world. Excessive liquidity at global level, fuelled by Asia’s foreign exchange reserves, helped create a housing and credit bubble whose burst has produced one of the most severe financial crises in history.

The crisis has also resulted from a lack of regulation in the financial system. While trade benefits from an effective system of multilateral rules, there is no such system for global finance. In particular, countries lack the ability to control the movement of capital across borders. Market mechanisms may work well in times of stable growth, but can also exacerbate problems in times of disruption.

A lesson of the crisis is the limits of the “Washington consensus”, which advocates strong reliance on market forces to spur economic development. The “Washington consensus” was introduced after two decades of heavy government intervention in the developing world, which had produced mixed results. Today, a rebalancing is needed to integrate the notion that governments must be present to help redress excesses or to intervene in difficult times. UNCTAD increasingly refers to the concept of the “enabling state” to reflect this notion.

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As the world economy moves further into uncertainty, emerging economies should be seen as part of the solution, provided a few important steps are taken. Dr Supachai described six ways in which Asia could contribute to resolving the crisis:

- 1) Asian economies need to increase domestic consumption. This will require the establishment of a stronger welfare system so that Asian consumers can feel freer to spend more and save less.
- 2) Asia needs to keep its markets open and push for a successful conclusion of the Doha Round of multilateral trade negotiations.
- 3) Deeper financial integration should be encouraged in Asia, possibly through the creation of an Asian Monetary Fund.
- 4) The Asian Development Bank should play a great role in lending to smaller economies, notably for financing transport and water projects. For this, the Bank needs to receive more funding.
- 5) Measures are needed to foster the growth of south-south trade, not just within Asia but also between Asia and other emerging regions.
- 6) Economic liberalization should be pursued, but with a greater focus on stability. The global financial system should allow for stronger controls of cross-border movements of capital.

Plenary session 2

The second plenary session was addressed by **William Overholt**, Senior Research Fellow at the Harvard Kennedy School of Government, who offered his analysis of the root causes of the financial crisis and its effects on Asian economies.

The three root causes of the crisis could be described as:

- a world awash with liquidity
- mismanaged financial institutions
- a crisis of corporate governance.

So far, governments have been focussing most of their efforts on the least important one (i.e., mismanaged financial institutions) while underestimating the fundamental importance of the other two.

Low interest rates and high savings levels in China and Japan created a massive influx of liquidity, leading financial institutions and governments, particularly in the United States, to take imprudent decisions. Remuneration incentives and pressure from shareholders encouraged chief executives to take excessive risks. This was not a problem of ethics or individuals, but a structural problem of corporate governance.

The crisis broke out in the United States in an economic climate marked by lax fiscal and monetary policies, and a weak regulatory framework. The early responses to the crisis were fairly inconsistent and contributed to aggravate the loss of confidence. A basic principle in times of crisis management should be to save only those institutions that are crucial to the stability of the system.

Looking at individual economies, Japan seems in a stronger position since its banks bought few US toxic assets. But they may suffer indirectly from the consequences of the crisis due to their exposure to falling equity prices. China rightly focused its priorities on domestic economic development, but its social problems remain serious and its economy needs to move from state-sponsored growth to one led by small- and medium-sized enterprises. Russia, unlike China, has let its geopolitical ambitions get entangled with some of its economic interests.

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The crisis has not discredited the market economy system but has clearly eroded the “Washington consensus”. There is a need for a serious re-think of the basic principles guiding economic development. More emphasis should be placed on regulation and sequencing, while avoiding protectionism.

On a global level, political leaders have to find a way to manage the abundance of liquidity in the world and the resulting cross-border liquidity flows, possibly through the creation of a new global oversight body or the establishment of a new mandate for the International Monetary Fund. It is also crucial for political leaders to carry the message that protectionist measures would only aggravate the crisis.

After each of the addresses in the plenary sessions, the participants divided into six-break-out groups. The topics and conclusions of the break-out groups are presented below.

The Global Financial Crisis and the Asia-Pacific

Moderated by Kenneth Courtis, founding Chairman of Courtis Global Capital

The financial crisis is similar to an earthquake. After the initial shock will come the aftershock. A lot of corporate refinancing is due to take place next year and it is not clear how this will be made possible in a period of credit crunch. Deflation is now a significant risk, meaning that consumers will postpone spending decisions and further depress global demand.

It took 25 years to build the global imbalances that led to the current crisis. The new regulatory structure which would emerge from a reform of the global financial system should address these imbalances and find ways to regulate the unregulated sectors of financial markets. On a short-term perspective, the key challenge is to restore confidence so that banks start lending again.

In many ways, it would be a shame to waste the opportunities created by the crisis. A lot of positive factors could come out of the new imperative for governments to stimulate demand and recreate the conditions for sustainable economic growth. The following steps could help boost demand and inject confidence in the global financial system:

- New corporate governance reforms to restore public trust in business;
- A global review of the rating agency system to address conflicts of interest;
- A meeting at the highest political level between Brazil, China, the EU, India, Japan and the US to unlock the Doha Round of global trade negotiations;
- Governments to provide a subsidy of 50% of the salaries of new hires in small and medium-sized enterprises for the next two years;
- A group of eminent persons to present a full report on pensions and health care to governments worldwide;
- The creation of a global trade watchdog to monitor protectionist actions;
- The suspension for two years of the mark-to-market accounting principle and, under strict supervision, the loosening of capital requirements for financial institutions;
- A huge fiscal stimulus to boost global demand, led by coordinated government action throughout the world.



Global Trade and the Asia-Pacific

Moderated by Jean-Pierre Lehmann, Professor of International Political Economy at IMD and Founder of the Evian Group

Rebuilding demand and confidence are the two necessary conditions for reviving world trade in the current context. Without demand, there will be no trade. Without finance, there can be no trade. The immediate priority is not to reform the current trade regime but to rebuild trade capacity. A new global trade agreement would do little to boost trade if exporters cannot get the letters of credit to finance their transactions.

The risk of protectionism is, however, very real and should be contained. The multilateral trading system, embodied by the World Trade Organization, has worked very well so far and could serve as a model for the global financial system. Still, the recent rise of bilateral trade agreements creates a feeling that business is not as supportive as it should be of the Doha Round of multilateral trade negotiations.

An injection of liquidity is needed to reinvigorate cross-border trade. But the flow of trade is being choked by a lack of trade financing that is a direct consequence of the financial crisis. Banks do not wish to extend credit. As a result, exporters are unable to finance their international trade transactions. Immediate action is therefore critical to help unlock liquidity and get trade flowing again.

One way to do this is for governments to provide additional guarantees to government-backed export credit insurance agencies, such as the scheme that the Hong Kong SAR government has implemented with the Hong Kong Export Credit Insurance Corporation. This will encourage banks to finance trade transactions with minimum risk.

In the mid-term, increased stability and greater respect for trade rules are needed to sustain world trade growth. Asian countries should continue to push for a rapid conclusion of the Doha Round and consider engaging in unilateral trade liberalization in areas which will help boost global demand.

China and the global economy

Moderated by Richard Wong, Professor of Economics and Deputy-Vice Chancellor and Provost at the University of Hong Kong

After 30 years of rapid economic development, China's economy is now very open and therefore not immune to the global recession. Chinese companies are now switching to "survival mode", with many layoffs on the horizon. The situation is difficult both for export-oriented companies and small enterprises trying to break into the domestic market.

One role for China, which still enjoys large foreign exchange reserves, could be to provide capital to areas which are pivotal to restoring confidence. Signs that China is moving in the right direction would contribute enormously to confidence-building in Asia and the rest of the world. In particular, China should pursue the liberalization of its financial services sector, develop a stronger welfare system to encourage Chinese consumers to spend more, and seek to improve predictability in its relations with trading partners.



Asia-Pacific and the US

Moderated by William Overholt, Senior Research Fellow at the Harvard Kennedy School of Government

It is estimated that a quarter of Hong Kong-owned factories in the Pearl River Delta and southern China are likely to close over the next two years as a result of the slowdown of US demand. The US economy, and US decisions, have an enormous impact on Asian entrepreneurs. If the US decides not to bail out its car industry, another tsunami will be underway for Asian exporters.

A huge stimulus package on a global scale would help put the world economy back on track. More consideration should be given on how to spend this money in a sustainable way. Asian economies are often asked to increase domestic consumption, but there is a degree of reluctance within Asian societies to import Western lifestyles which are seen as a cause of the current crisis.

From an Asian perspective, the US could take a few important steps to strengthen its relationship with Asia:

- Get its own house in order: confidence cannot be restored until the US fixes its monetary, fiscal and regulatory policies.
- Take Asia more seriously: in particular, global institutions (e.g., the World Bank, the IMF, and the G8) should better reflect the new scale of Asia.
- Adopt a pragmatic approach to international economic issues through a re-think of the "Washington consensus".

Asia-Pacific as a Community

Moderated by Clyde Prestowitz, Founder and President of the Economic Strategy Institute

It is difficult to speak of an Asian community as there are large political, economic and ethnic differences within Asia. The concept of "decoupling" Asian economies from the rest of the world is largely a myth, since a significant part of Asian business consists of supply chain trade in which the final customer is based in the US or Europe. Only countries belonging to the Association of South East Asian Nations (ASEAN) can be seen as a community since they have achieved a higher degree of integration.

While much attention is currently focussed on China, Japan remains the largest economy in the region and the second largest in the world. The role of Japan in providing an alternative source of demand for the world economy is often overlooked. It is important for Asia as a whole to stimulate domestic demand, since Asia will not be able to export its way out of the crisis this time. The concept of "growing the bottom of the pyramid" could be successfully applied in Asia as a way to enable millions of low-income consumers to participate in the development of strong domestic economies.

One way to strengthen the Asian voice would be to combine the myriad of Asian organizations and regional agreements into one single Asian economic association. Such movement could start with the establishment of business organizations on a regional level, e.g., an Asian automobile industry federation. A key message the Asia-Pacific community could carry is that the process of globalization should continue, but in a better regulated way.



Climate change and the Asia-Pacific
Moderated by Martin Wassell, ICC First Director

Despite the historical reality that Europe and North America are mainly responsible for the current situation, it is clear that climate change has now become a global problem in need of a global solution. Environmental awareness is not as developed in Asia as in the Western world, where political parties and non-governmental organizations have largely contributed to raise the public's attention to the issue of climate change.

The role of business and governments in this area is not clearly delineated, and in many ways Asian enterprises lack the necessary incentives to integrate climate change into their business strategies. Some also perceive a risk that the financial crisis will lead managers to squeeze production costs, and that environmental issues such as climate change will get pushed off the agenda as a result.

But the financial crisis also provides a unique opportunity for Asia and other regions to address climate change, as governments will now be looking for ways to stimulate economies. Investment in clean technologies and resource efficiency could help increase demand for environmental goods and reduce energy costs for businesses and consumers. Improving environmental management, especially in SMEs, is an area in which ICC could play a helpful role through the development of common voluntary standards.

At the conclusion of the meeting, ICC Secretary General **Guy Sebban** stressed that ICC was not only the voice *of* business but also a voice *to* business. A new objective for ICC was now to integrate regional approaches into its work, with a view to provide a stronger voice for businesses from all parts of the world. Fighting protectionism and pushing for a rapid conclusion of the Doha Round remained top priorities for ICC, in addition to developing valuable and actionable proposals for reconstructing the global financial system.

ICC Chairman **Victor K. Fung** thanked all the participants and assured them of ICC's strong commitment to defending open markets, contributing to the resolution of the financial crisis, and integrating more Asian companies into its rule-making and policy advocacy work. He emphasized that one of the greatest strengths of ICC was its power to convene, both at a global and local level, and that this convening power provided a great channel for business to contribute solutions for today's global challenges.