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# Commentary

BUFFIN PARTNERS INC. ECONOMIC INVESTMENT AND ACTUARIAL RESEARCH

## The G-20 Toronto Commitments

The recent G-20 summit meeting in Toronto produced a number of major commitments that will have a significant impact on future global economic growth and financial stability. The Joint Declaration issued by the G-20 nations at the close of the meeting described the next steps to be taken to ensure a full return to balanced and sustainable economic growth, together with measures to reform and strengthen financial systems. Although globally-coordinated fiscal and monetary stimulus programs are helping to restore private demand and lending, the G-20 noted the importance of continuing the efforts with existing stimulus programs. An objective was set of achieving sustainable public finances with phased growth plans tailored to differing current national circumstances. The G-20 also committed to developing a better-regulated and more resilient financial system.

It was agreed that sound fiscal finances are essential to sustain recovery, provide flexibility to respond to new shocks, ensure the capacity to meet the challenges of aging populations, and avoid leaving future generations with a legacy of deficits and debt. Concerted global actions are necessary with fiscal stimulus programs to sustain the economic recovery process, create jobs and achieve more balanced growth. However, the G-20 noted that synchronized fiscal adjustments across several major economies could adversely affect the recovery process. For advanced deficit countries the G-20 advocates action to boost national savings while maintaining open markets and enhancing export competitiveness. For advanced surplus economies the G-20 advocates reforms to reduce reliance on external demand and an increased focus on domestic sources of growth. For emerging surplus economies the G-20 advocates a wider range of actions, including: strengthening social safety nets such as public health and pension plans; increasing infrastructure spending to help boost productive capacity; and enhancing exchange rate flexibility to reflect underlying economic fundamentals.

The G-20 made significant commitments at the Toronto meeting for financial sector reform. The joint declaration emphasized the need to build a more resilient financial system that better serves the real needs of national economies, reduces the exposure to moral hazard, limits the build-up of systemic risk and supports strong and stable economic growth. Progress in strengthening the global financial system requires more effective prudential oversight, improved risk management, greater transparency, and fuller international cooperation. The core of the G-20 financial sector reform agenda rests on improving capital and liquidity and avoiding excessive leverage. Accordingly the G-20 nations collectively agreed to increase the quality, quantity, and international consistency of capital, to strengthen liquidity standards, to discourage excessive risk taking and leverage, and to reduce the effects of economic cycles. The Basel Committee on Banking Supervision is making progress towards a new global regime for bank capital and liquidity that will result in significantly higher amounts of capital while the quality of capital will be substantially improved so as to reinforce the banking sector's ability to absorb losses. A new capital framework that is anticipated to be agreed at the next G-20 summit meeting in Seoul would establish a new requirement that each bank hold adequate fully-loss-absorbing capital, so as to meet stresses of the magnitude that were experienced during the recent financial crisis, without extraordinary government support. As agreed at the previous G-20 Pittsburgh meeting, new standards under Basel II will be adopted in all major centers by 2011; these standards will be phased in over a timeframe that is consistent with sustained recovery and that limits market disruptions.

The G-20 agreed that new and stronger rules must be complemented with more effective oversight and supervision. The Financial Stability Board, in consultation with the International Monetary Fund, will recommend procedures to accomplish this objective. These procedures will specifically relate to the mandate, capacity and resourcing of supervisors, and will provide the essential powers necessary to identify and address risks, including early intervention authority. The G-20 also committed to adopt measures to reduce moral hazard in the financial system and to implement systems with the powers to restructure or resolve financial institutions in crisis, so as to avoid taxpayers ultimately bearing the burden of future potential crises. Resolution regimes should provide: the proper allocation of losses to reduce moral hazard and protect taxpayers; the continuity of critical financial services; credibility in the market; minimization of contagion effects; advance planning for orderly resolution and transfer of contractual relationships; and effective cooperation and information exchange in the event of a failure of a cross-border institution. The G-20 agreed that the financial sector should make a fair and substantial contribution towards paying for any burdens associated with government interventions to repair the financial system or to fund resolution actions. A range of feasible policy approaches are being studied, including the imposition of levies. The guiding principles for these studies are: protection for taxpayers; reduction of risks in the financial system; and maintaining the flow of credit.

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