2015 G20 Think Tank Summit

Chongyang Institute for Financial Studies
Renmin University of China
30 July – 1 August 2015
Beijing, China

THE GLOBAL GROWTH CHALLENGE, THE G20 GROWTH STRATEGIES AND THE CHINESE PRESIDENCY

Adam Triggs

East Asian Bureau of Economic Research, Graduate Scholar, Crawford School of Public Policy, Australian National University.

Abstract

This paper looks at how China could use its G20 presidency in 2016 and the G20 growth strategies to better address the global growth challenge. Since at least 2011, the IMF's forecasts for global growth have been repeatedly downgraded. The G20 has sought to address this by developing the G20 framework for strong, sustainable and balanced growth and more recently the G20 growth strategies and the goal of lifting G20 GDP by 2 per cent by 2018. This paper outlines the challenges China will face in 2016 in terms of global growth, the growth strategies and the 2 per cent growth goal. These include a declining baseline for growth, key reforms not being implemented, less-fortuitous political cycles and deficiencies in the mutual assessment and peer review processes. This paper proposes some practical suggestions on how these challenges could be overcome, including better targeting the structural reforms in the growth strategies to the global growth challenge, having a stronger complementary focus on jobs and macroeconomic policies, developing a more streamlined growth strategy process, better integrating the peer review mechanism throughout the G20 and improving G20 engagement with the public to boost accountability and lift ambition.

1. Introduction

This paper looks at how China could use its G20 presidency in 2016 and the G20 growth strategies to better address the global growth challenge. The best G20 agendas are those that address fundamental challenges facing the global economy while also resonating with the strengths of the G20 president so it can demonstrate leadership on those issues. In light of the significance of the global growth challenge and China's unparalleled leadership in undertaking bold and difficult structural reforms, a focus on the global growth challenge in China's G20 presidency ticks both these boxes.

Since 2011, the IMF's global growth forecasts could be called 'the growth that never comes'. These forecasts have not materialised and have been repeatedly downgraded, including the IMF's most recent forecast in July 2015. In 2009 the G20 launched the framework for strong, sustainable and balanced growth in an effort to secure commitments from G20 countries to address this global growth challenge. In 2013 and 2014, G20 countries developed comprehensive growth strategies with the goal of lifting G20 GDP by 2 per cent by 2018. While analysis from the IMF and OECD in 2014 suggested the growth strategies could achieve this goal, the G20 faces a number of serious challenges which will need to be addressed when China assumes the G20 presidency in 2016.

First, the baseline for the G20's 2 per cent growth goal is in decline. The G20 set the IMFs October 2013 World Economic Outlook (WEO) as its baseline but since then the IMF has repeatedly downgraded its forecasts for G20 GDP. Second, a number of critical reforms in key countries are not being implemented meaning new reforms will be required to fill this gap. Third, there is reason to believe the level of ambition among G20 members may be lower in 2016 given political cycles may be less fortuitous than when the strategies were developed in 2014. And finally, there are deficiencies in the G20's processes for mutual assessment and peer review which make filling these growth gaps more difficult.

This paper proposes some practical suggestions for the incoming Chinese presidency on how these challenges could be overcome. The temptation for any new G20 president is to overhaul existing processes and the agenda to stamp their own identity on the G20, while also trying to reignite the ambition of members by rejuvenating the process through which they make commitments. The downside of this approach is the plethora of 'strategies' and 'action plans' that it generates as well as confused public messaging, diluted focal points and an ever-expanding and changing G20 agenda.

Instead, the Chinese presidency should focus on using the existing growth strategy process to maintain continuity and credibility towards the 2 per cent growth goal but fine-tune the process in a number of ways. This includes better targeting the structural reform themes of the growth strategies to the global growth challenge, having a stronger complementary focus on jobs and macroeconomic policies, developing a more streamlined and efficient process in getting and implementing commitments from members, better integrating the peer review mechanism throughout the broader G20 process and improving G20 engagement with the public to boost accountability and lift ambition.

2. The G20's approach to the global growth challenge

There are many ways to characterise the global growth challenge, but one way is to look at the IMF's forecasts for global growth over time. Figure 1 shows 'the growth that never comes'. It shows that the IMF's growth forecasts have not materialised and have been repeatedly downgraded. The latest WEO update for July 2015 continues this trend, representing a -0.2 percentage point downgrade for global growth in 2015. Although 2016 remains unchanged at 3.8 per cent, risks are firmly tilted to the downside. While growth is picking up in the US, there are continuing challenges in the euro area, weak global investment, slowing growth in emerging market economies and uneven global growth which, in most countries, is still too weak to bring down the legacies of high debt and high unemployment from the Great Recession.

Figure 1: The growth that never comes – IMF global growth forecasts since April 2011

Source: IMF WEO databases, April 2011 – April 2015

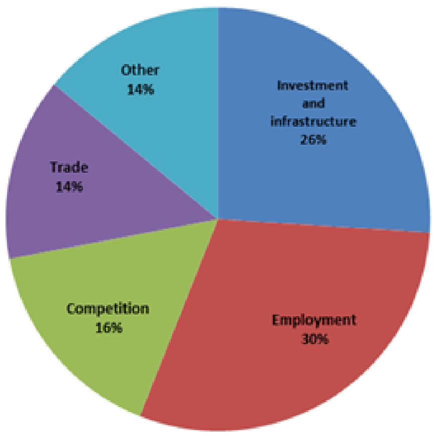
The G20's response to this global growth challenge has moved through phases and continues to do so. In 2008 and 2009 the focus was squarely on crisis-response through coordinated fiscal and monetary stimulus. But in Pittsburgh in late 2009 the G20 took its first decisive step in focusing on this longer-term global growth challenge by launching the G20 framework for strong, sustainable and balanced growth. The purpose of the framework is to ensure that members' domestic policies are not only consistent with global growth objectives, but that members are actively encouraged to implement policies in pursuit of those objectives (G20 leaders, 2009, para 5).

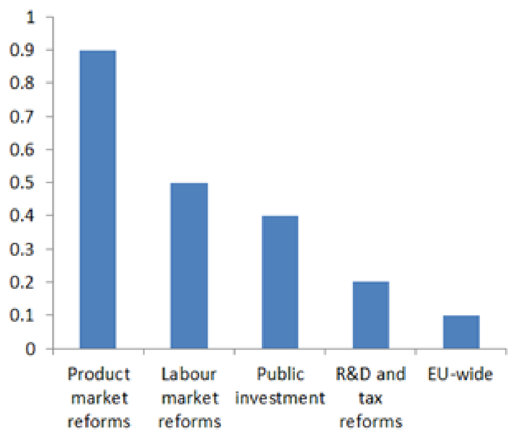
The framework exists through a mechanism known as the mutual assessment process (MAP) where each country puts in a submission outlining its domestic policies and how they help achieve 'strong, sustainable and balanced growth'. The IMF aggregates these submissions and presents a baseline scenario for growth and other key indicators as well as a more aspirational upside scenario which could be achieved through more ambitious reforms. Members discuss and peer review each other's MAP submissions through the Framework Working Group. Each country's submission is peer reviewed by two other countries. The G20 relies on this peer review process, as well as the analysis from the international organisations, in enforcing its commitments.

The biggest change to this process started in 2013 under Russia's presidency. Leaders agreed that by the time of the Brisbane summit in 2014 each country would develop a growth strategy including measures to improve domestic environments for investment in infrastructure and measures to boost employment and participation (G20 leaders, 2013, para 22). In early 2014 under the Australian presidency, officials added two additional themes: measures to boost trade and measures to boost competition. At their meeting in Sydney in February 2014, finance ministers and central bank governors agreed to the goal of using the measures in the growth strategies to lift G20 GDP by 2 per cent by 2018 (G20 finance ministers, 2014, para 3). The IMF and OECD presented updates throughout 2014 on progress towards this goal and the FWG and mutual assessment process was used to peer review the strategies and encourage ambitious reforms from the membership.

At the Brisbane summit leaders announced that the goal had been achieved. The collective impact of the growth strategies was estimated by the IMF and OECD to lift G20 GDP by 2.1 per cent by 2018 (G20 leaders, 2014). Overall a total of about 1000 commitments were made through the growth strategies process, about 800 of which were assessed to be new, meaning they were announced after the St Petersburg summit in 2013. The bulk of these reforms were in relation to investment and infrastructure and employment (Figure 2). The reforms which had the biggest growth impact were product market reforms followed by labour market reforms (Figure 3).

Figure 2: Number of commitments by theme **Figure 3: Contributors to the 2 per cent goal**

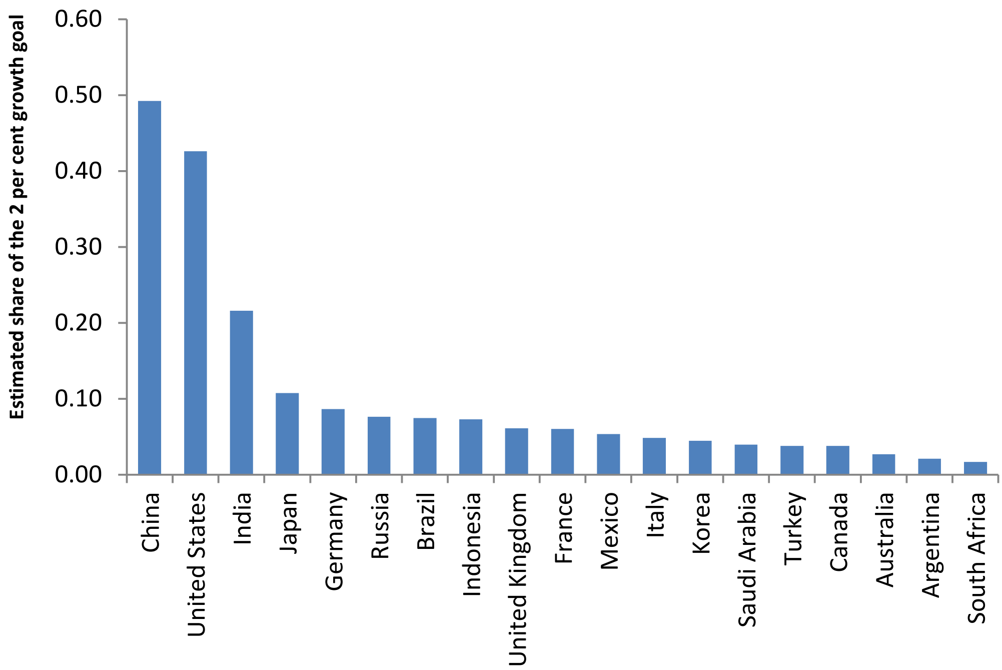




Source: IMF and OECD, November 2014

Although it was never made public how countries ranked in their contribution to the 2 per cent growth goal, members' shares of G20 GDP gives a rough idea of where the bulk of this growth would need to come from for the goal to have been achieved. Figure 4 suggests at least a quarter of the 2 per cent growth goal would have come from China and about the same (around one-fifth) from the US, followed by India, Japan, Germany and Russia. The growth strategies of these larger countries would therefore have been critical to the success of the G20 growth strategies process.

Figure 4: Estimated shares of the 2 per cent growth goal based on members' shares of G20 GDP (PPP)



Source: IMF WEO, April 2015

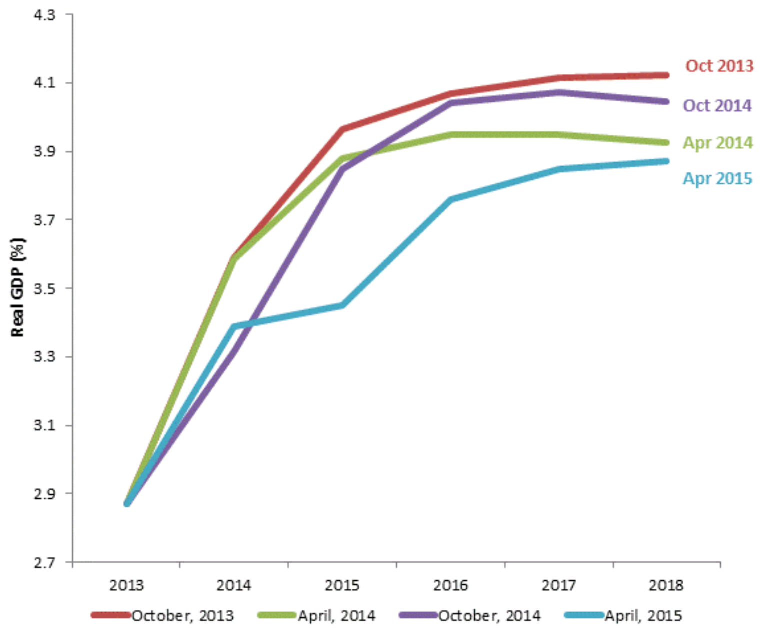
3. The challenges facing the G20 growth strategies in 2016

The G20 faces a number of challenges which will need to be dealt with when China assumes the presidency in 2016. These include a declining baseline for the 2 per cent growth goal, a number of critical reforms in key countries not being implemented, potentially lower ambition from the membership due to changing political cycles, the adequacy of the peer review process and the impact of constant changes to the framework and mutual assessment process.

A weakening baseline and key reforms not being implemented

Figure 5 illustrates an important challenge China will face in regards to the G20 growth strategies and the goal of using them to lift G20 GDP by 2 per cent by 2018. The baseline for measuring the G20's 2 per cent growth goal is the IMF's growth forecasts in October 2013. However Figure 5 shows that since then the IMF has downgraded its forecasts for G20 GDP multiple times meaning the additional 2 per cent of growth is proving to be much harder to achieve.

Figure 5: IMF downgrades to G20 GDP since the October 2013 baseline



Source: IMF WEO databases

This presents at least two problems. First, it shows that the G20 membership will need to produce even more reforms if it is to achieve its 2 per cent growth goal. But second, it also suggests the IMF is perhaps sceptical about whether G20 members will actually undertake the reforms they have committed to given the 2 per cent growth goal does not appear to have been reflected in their forecasts. Although it is unclear whether this is the case or not, failure to implement key reforms can be seen in a number of countries.

In the US, the Obama Administration has been unable to secure Congressional approval for its immigration reform package, having instead to rely on the President's Executive Power which could be reversed following the 2016 election. This package is estimated by the Congressional Budget Office to lift US GDP by 3.3 per cent by 2023 (United States G20 growth strategy, 2014, p15) which would represent a sizeable chunk of the G20's 2 per cent growth goal. Similarly in Australia (which was the G20 president overseeing the growth strategies process in 2014) a number of reforms are not being delivered, including a new paid parental leave scheme, higher education reforms, reforms to Medicare and GP co-payments and a potentially weaker infrastructure investment through the impact of state government elections on its asset recycling initiative (Australia G20 growth strategy, 2014).

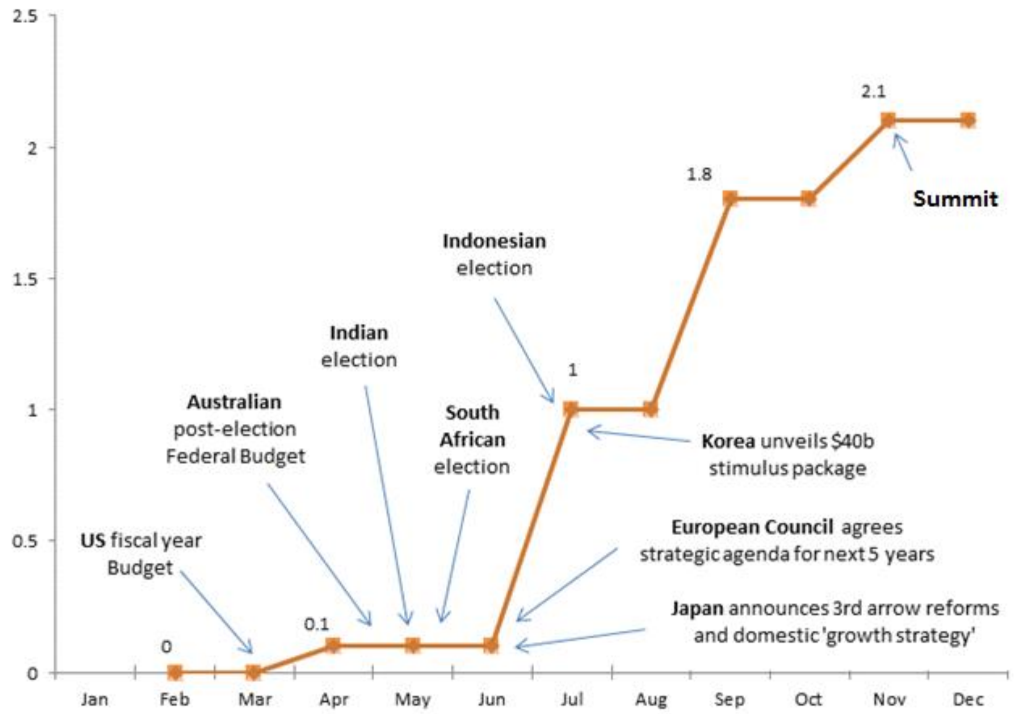
Furthermore, the Macroeconomic and Reform Priorities Report prepared by the IMF, OECD and World Bank details a number of the assumptions that underpin the 2 per cent growth goal being achieved. These include a fully flexible exchange rate in China and a large increase in public investment in Germany (IMF, OECD, World Bank, 2014). Countries will be continuing to add to their growth strategies in 2015 but time will tell whether the growth gaps left by these reforms have been filled.

The level of ambition among members and the ability of peer review to increase it

The G20 growth strategies are only as strong as the political will of individual countries. A fundamental question for the growth strategies process in 2014 is to what extent it delivered reforms that would not have been delivered anyway. There is a risk that the level of ambition that was demonstrated during Australia's G20 host year was the product of fortuitous political cycles among the membership rather than the growth strategies process itself such that this level of ambition may not be repeated in 2015 or 2016.

For example, the majority of the reforms contained in the US growth strategy come from the 2015 fiscal year Budget, the first to be passed by Congress in some time. This was similarly the case for Australia with most of Australia's reforms coming from the Abbott Government's ambitious first post-election Budget. Similarly, the reforms contained in the growth strategies of India, Indonesia and South Africa replicate the commitments coming out of the election campaigns in those countries. The domestic growth strategy announced by Japan, the fiscal stimulus announced by President Park in Korea and the European Council's agreement of its strategic agenda for the next 5 years were all well-timed in delivering commitments for the 2 per cent growth goal (Figure 6).

Figure 6: Political cycles in 2014 and estimates of G20 progress on the 2 per cent goal throughout the year



Source: Ministerial communiques and press releases in 2014

Of course, just because the reforms in the growth strategies replicate those coming out of elections and budget processes does not necessarily mean the G20 did not play a role. Truth is, the counterfactual will never be known. But the risk is that the level of ambition demonstrated in 2014 may not be replicated in future years given that political cycles may not be as favourable. This is a problem given the need for additional reforms to fill the gaps left by reforms not being implemented. In particular, an important issue will be what effect the presidential election has on how engaged and ambitious the US will be during China's G20 presidency. On the one hand it could mean a lame duck US given any new reforms cannot be announced until after the election, which roughly coincides with the end of China's G20 presidency. But on the other hand, the Obama Administration has so far shown it is far from being a lame duck in a number of important policy areas which could mean the US may be more ambitious than is usually the case at this point in its election cycle. However the reliance on Executive Power in implementing many of these reforms means they are at the mercy of the new incoming president.

The ambition of G20 members is not only a product of political cycles but also the effectiveness of the mutual assessment process, peer review and analysis from international organisations in pushing members to do more. The risk with this is that the peer review process has a tendency to become a 'tick and flick' exercise where countries will simply recommend their peer review partners undertake the reforms that have already been recommended for years by the IMF through its article 4 consultations and the OECD through its Going for Growth reports. The peer review process also tends to be compartmentalised within the Framework Working Group with little to no engagement at the level of finance deputies, sherpas, ministers or leaders which are the individuals that tend to carry the most weight in influencing the level of ambition across the membership. The development of the growth strategies process has helped address some of these problems but there is scope for more to be done during China's G20 presidency.

Constant changes to the process and 'strategy fatigue'

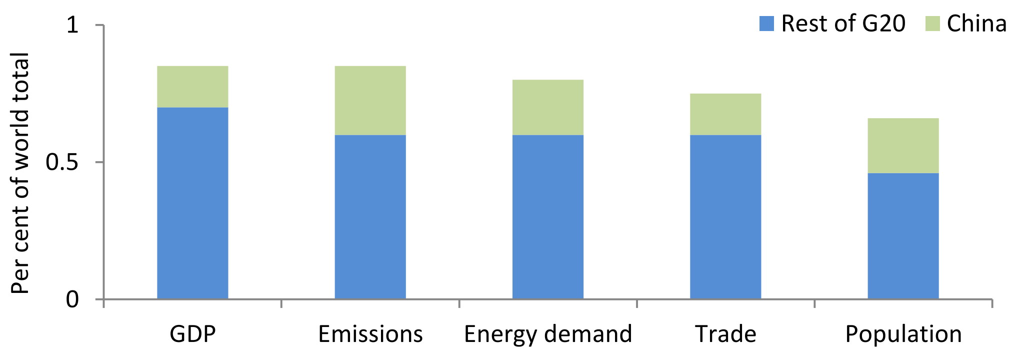
There is another challenge around constantly changing the process of how G20 commitments are made over time. The G20 has developed an unfortunate habit of priding itself when members put forward hundreds of new commitments and then, in the following year, priding itself on thinning out what are then deemed to be commitments of little value so as to make the process more targeted and streamlined. For example, the presidencies of France (2011) and Mexico (2012) saw a large increase in the number of MAP commitments. In response, Russia in 2013 used its presidency to streamline those commitments to focus on those with the most significant growth impact. However, Australia then introduced the growth strategies process which saw commitments blow-out from around 200 under Russia to about a 1000. In response, Turkey has said its presidency in 2015 will focus on implementation and that these efforts would only focus on the commitments with the most significant growth impact (G20 finance ministers, 2015, para 7). There is clear scope here for the G20 to bed-down a process for the longer-term, or at least until the outcome of the 2 per cent growth goal is judged in 2018.

Related to this, there is a risk that 'strategy fatigue' sets in among G20 members which acts to further reduce the level of ambition among members, let alone the interest of politicians and their electorates. As of 2015, the G20 now produces leaders' communiques, ministerial communiques, G20 action plans, G20 fiscal strategies, G20 growth strategies, G20 investment strategies and G20 employment plans as well as individual action plans on anti-corruption, energy efficiency, financial inclusion and remittance flows. This expansion in the number of strategies and action plans risks diluting focal points, creating confused messaging and encouraging an ever-expanding G20 agenda.

4. Responding to these challenges in China's presidency

As said at the outset, the best G20 agendas are those which address fundamental challenges facing the global economy but also resonate with the domestic agenda of the G20 president so it can demonstrate leadership on those issues. A focus on the global growth challenge by the Chinese presidency ticks both boxes. Even though there are green-shoots, global growth remains too weak and uneven and, with limited macroeconomic policy space in some countries, this means there must be a greater focus on structural reform. Similarly, China is engaged in genuine and deep structural and market reform and will have great authority in leading on this issue and getting others to reform their own economic systems for the mutual good. China's Third Plenum outlines a comprehensive package of broad and detailed reforms to be implemented, particularly around capital account liberalisation. And as Figure 7 shows, China is critical to the G20 on so many fronts and is extremely well-placed to discuss the range of issues facing the global economy.

Figure 7: The importance of China to the G20



Source: IMF WEO (April 2015), World Bank (2014), BP (2014), WTO (2014), UN (2012)

The temptation for any new G20 president is to overhaul existing processes to stamp their own identity on the G20, while also trying to reignite the ambition of members by rejuvenating the process through which they make commitments. The downside of this, as discussed, is the plethora of strategies and action plans it generates, confused messaging and diluted focal points and an ever-expanding G20 agenda. Instead, the Chinese presidency should use the existing growth strategy process to maintain continuity and credibility towards the 2 per cent growth goal, but fine-tune the process so it is better targeted to the global growth challenge, better targeted to the issues in which China can demonstrate leadership, more streamlined and efficient in securing commitments from members and resonating more effectively with the public.

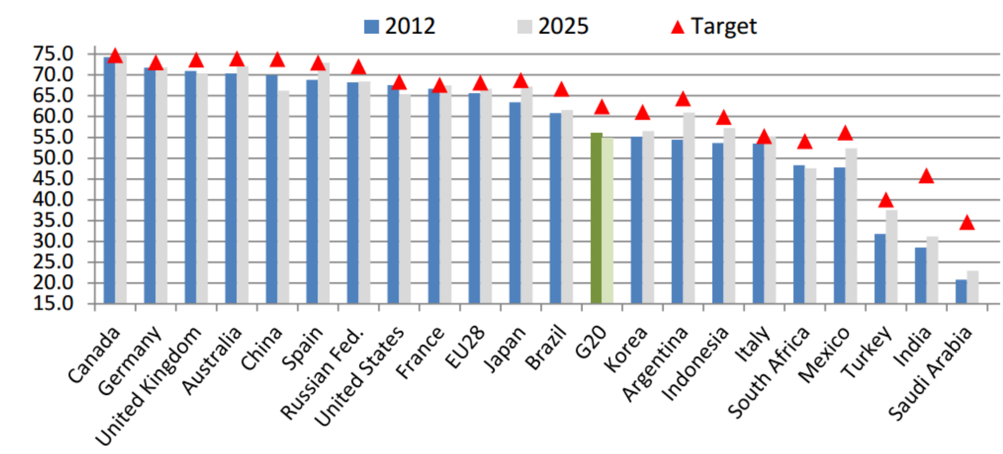
Better targeting the structural reform themes of the G20 growth strategies

The four structural reform themes of the G20 growth strategies are investment and infrastructure, employment, competition and trade. Rather than adding more themes or removing existing ones, there is scope to better target these themes to areas that have substantial growth potential which thus far have been neglected by the membership. The G20 has delivered a substantial body of structural reform commitments over many years. But many of these reforms are not the sorts of reforms that improve the ease of doing business or unleash business investment. Private sectors around the world continue to sit on large amounts of cash, holding back on investing in additional productive capacity.

Reforms on investment and infrastructure could be better targeted in three ways. First, there needs to be a stronger focus on the private sector. The vast majority of reforms listed in the growth strategies consist of increased public investment while there is an insufficient focus on the institutional and regulatory reforms that would better leverage private investment and facilitate public-private partnerships (PPPs). India and Indonesia are two examples of countries which have included solid reforms to institutional settings to help encourage PPPs. Second, while there needs to be a greater focus on private investment, the IMF has also highlighted that for many countries there is scope for an increase in public investment in infrastructure, including through deficit spending for countries facing historically low long-term interest rates. And third, there is scope to better connect the range of international institutions which are all working independently on increasing infrastructure investment, including the Asian Infrastructure Investment Bank, the World Bank's Global Infrastructure Facility, the G20's Global Infrastructure Hub as well as the work of multiple multilateral development banks. There are clear synergies which could be gained through a more cohesive approach across these institutions.

For employment, the growth strategies need a stronger emphasis on participation. The majority of the employment reforms listed in the growth strategies tend to be smaller scale employment programs rather than larger-scale reforms that will have a tangible effect on lifting participation which is critical to growth. This is, of course, inextricably linked to reforms to create more jobs as well as macroeconomic policies discussed in the next section. However the G20s commitment on female participation – to close the gap between male and female workforce participation by 25 per cent by 2025 ('25 by 25') – provides a ready-made framework for a greater participation focus (G20 leaders, 2014, para 9). This commitment will be harder for some countries to achieve than others, as shown in Figure 8. But the OECD has estimated that achieving '25 by 25' would add 100 million women to the global workforce and increase G20 GDP by a full 1.6 per cent, more than three-quarters of the 2 per cent growth goal with this single commitment (OECD, 2014b).

Figure 8: G20 country comparisons against the '25 by 25' female participation goal



Source: OECD, ILO, IMF and World Bank (2014)

On competition, analysis from the OECD shows there is significant growth potential in delivering additional product market reforms. Competition and product market reforms represent only 16 per cent of total G20 commitments but account for almost half of the 2 per cent growth goal (see Figures 2 and 3). The OECD estimates a 10 per cent reduction in the level of product market regulations can permanently boost GDP by between 1 and 1.5 per cent (OECD, 2014). A practical commitment in this area would be for each G20 country to undertake a sweeping review of national and sub-national laws and regulations to assess their effects on competition, productivity and growth. The OECD has developed a detailed Competition Assessment Toolkit which could act as the framework for undertaking these reviews. By way of example, Australia undertook such a national-wide assessment in 1993 and, implementing these recommendations from 1995 to 2005, permanently lifted Australian GDP by 2.5 per cent (Productivity Commission, 2008).

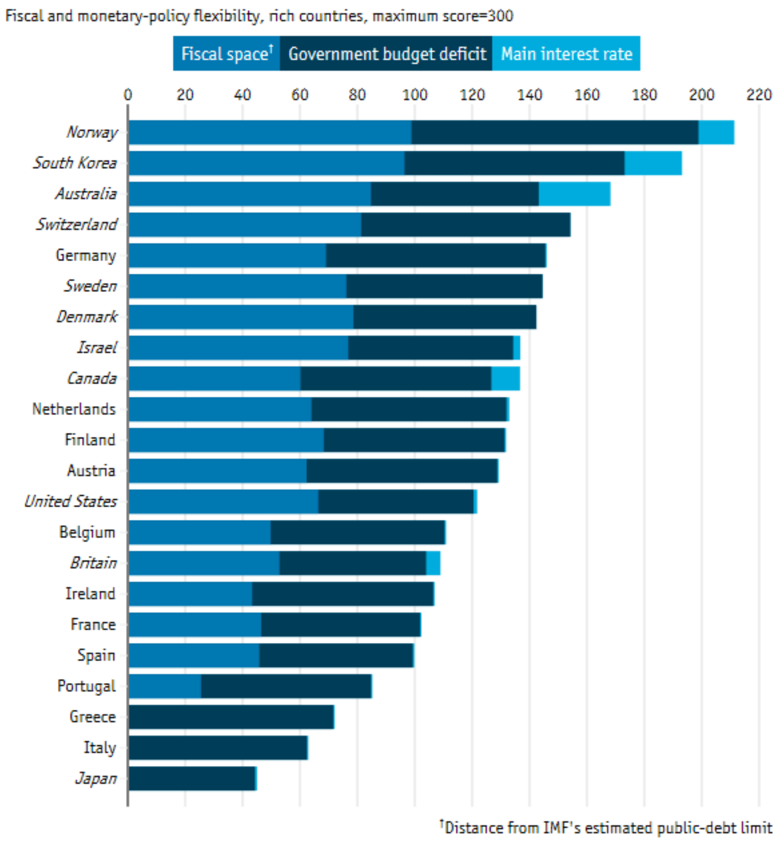
Finally on trade, there is scope for countries to do more to facilitate trade through behind the border reforms. These trade reforms are inextricably linked to the competition and product market reforms discussed above and could be dealt with under the same national and sub-national review framework. Similar to linking the G20 infrastructure agenda with regional initiatives like the AIIB, there is scope to link the G20 trade agenda and its focus on behind the border structural reform with the ASEAN+6 Regional Comprehensive Economic Partnership (RECP). RCEP can help regionalise Asia's sophisticated global production networks (Wignaraja, 2013). It will also reduce the complex overlap among Asian FTAs and, not only provide a framework for mobilising middle powers to strengthen regional institutions, but aspire to be a model for a global set of principles-based rules for managing trade and other forms of international commerce (Drysdale, 2014).

A stronger complementary emphasis on jobs and macroeconomic policy

Early in 2014 the OECD presented some of its estimates around the 2 per cent growth goal, saying it would increase global GDP by US$2 trillion and create around 18 million new jobs (OECD, 2014b). While the US$2 trillion growth figure was included in the final communique from leaders in Brisbane, the absence of any estimates around job creation suggests that more could be done in this area. A more specific focus on job creation is also crucial for engaging the interest of leaders and ministers. While much of this job creation is connected to reforms on investment and infrastructure, labour market reform and liberalisation of product markets and trade, it is also linked to what the US suggests has been recently missing from the G20, and that is an adequate focus on reforms to lift aggregate demand (Lew, 2015).

Lifting aggregate demand entails not only confidence-building structural reforms to unlock private sector investment but also having more G20 countries using available macroeconomic policy space to support growth in the short-term. The Economist's famous 'wiggle-room' ranking (Figure 9) measures macroeconomic policy space in terms of public debt (fiscal space), budget deficits and interest rates. A number of G20 countries rank highly, including Korea, Australia, Germany and Canada. This supports calls from the IMF for more G20 countries, including those listed, to use available macroeconomic policy space as well as historically low long-term interest rates to invest in much needed infrastructure to support growth and job creation (Lagarde, 2014).

Figure 9: The Economist's 'wiggle-room' ranking



Source: The Economist, 13 June 2015

Streamlining the growth strategies process

There are a number of ways the growth strategy process could be streamlined so as to improve the clarity of messaging and reduce unnecessary bureaucracy. First, the G20 employment plans were an important outcome of the meeting of labour ministers in 2014, but they are largely duplicative of the growth strategies which already have a dedicated theme on employment policies. The G20 employment plans should be rolled into the growth strategies, or if they do continue, should simply be used as a mechanism for the Employment Working Group rather than a leader-level announceable which tends to create confusion.

Second, the G20 investment strategies should be rolled back into the investment theme of the growth strategies. Lifting global investment is a fundamental issue and Turkey is right to have a special focus on it. But going forward this work should form part of the growth strategies process, particularly given the need to focus on implementation and accountability after Turkey's presidency. Finally, the St Petersburg fiscal strategies developed under the Russian Presidency added much value in focusing the G20's attention on the need for fiscal policy to support growth in the short-term within a sound medium-term framework. But rather than treating fiscal policy as its own separate issue, these strategies should now be rolled into the broader macroeconomic policy theme of the growth strategies discussed above.

Better integrating the peer review process

The peer review process has a tendency to become a 'tick and flick' exercise largely isolated to the Framework Working Group with limited engagement of finance deputies, sherpas, ministers and leaders. Given peer review is the primary mechanism the G20 relies upon for the enforcement of its commitments it makes sense that it should be much more integrated throughout the broader process. The peer review process that takes place within the FWG should be replicated at the level of finance deputies, sherpas and ministers. To date, when members at this level have specific remarks about the policies of another member they have no choice but to raise it during general discussions about that policy issue. Having a specific session on peer review provides a designated opportunity for these sorts of discussions to take place. The FWG could also adopt a panel of eminent experts from outside the G20 community to provide practical suggestions on the individual growth strategies of members (see Vines, 2014 and Ostry and Ghosh, 2013). Providing such practical and specific recommendations is something that an independent panel of experts can do more easily than other G20 members and the international organisations.

Improving G20 engagement with the public

The ambition and implementation of leaders' and ministers' commitments depends on their being held accountable by other G20 countries through peer review as well as being held accountable within their own country through better engagement with the public. Strengthening public engagement not only means strengthening accountability over existing commitments but also lifting the ambition of leaders and ministers in making future commitments. Much of this relies on having effective media strategies, public events and strong political engagement from leaders and ministers. While public engagement tends to be high within the country that is hosting the G20 (or is about to), public engagement tends to be much lower within other G20 countries. An option to address this is to have countries formally outline through the peer review process what actions they will take to engage with their public on the reforms in their growth strategy and how the actions of their country will help contribute to the G20's global objectives. Such actions could include specific media interviews, public events, roundtables, forums with academic experts and media campaigns and advertising.

5. Conclusion

A focus on lifting global growth resonates with both the key challenges facing the global economy and the strengths of the Chinese presidency in 2016. The G20 has articulated a 2 per cent growth goal and through the G20 growth strategies has developed a vehicle that can get there. But this paper has outlined a number of challenges which the Chinese presidency will need to address if this goal is to be achieved. These include a declining baseline, key reforms not being implemented, less-fortuitous political cycles and deficiencies in the mutual assessment and peer review processes.

The paper has proposed some practical suggestions on how these challenges could be overcome, including better targeting the growth strategy themes to the global growth challenge, having a stronger focus on jobs and macroeconomic policies, developing a more streamlined growth strategy process, better integrating the peer review mechanism throughout the G20 and improving G20 engagement with the public to boost accountability and lift ambition.

None of these suggestions will be easy to implement. Preceding G20 presidents tend to be very attached to the processes, goals and strategies they helped create. However failure to achieve the 2 cent growth goal and to make a significant dent into the global growth challenge would be far more difficult for the G20 to explain. It would very damaging to the G20's credibility, particularly as it tries to carve-out its post-crisis 'peace-time' role which is fundamentally about promoting jobs and growth in the medium to longer-term. China is engaged in genuine and deep structural and market reform which puts it in a powerful position to lead the G20 in addressing these challenges.

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