



Berlin, 21 November 2004

G-20 ACCORD FOR SUSTAINED GROWTH

Stability, Competition and Empowerment: Mobilising Economic Forces for Satisfactory Long-Term Growth

We, the Finance Ministers and Central Bank Governors of the G-20, have a common goal of promoting employment, welfare and development in our countries. We are convinced that strong and sustained economic growth is necessary both at national and global level to achieve this end. We have therefore discussed the requirements for long-lasting growth on the basis of our own experience and believe that domestic policy needs to address three tasks: establishing and maintaining monetary and financial stability; enhancing domestic and international competition; and empowering people to participate. Transparency and accountability within an internationally agreed framework of codes and standards remain key to ensuring sustained economic growth and stability at the global level. We agreed on the following key elements that will guide our domestic economic policies in the future. In implementing these elements, microeconomic aspects must be given due consideration. As these principles are interlinked, they must be implemented consistently, with due regard to possible trade-offs and complementarities, because many single elements have the potential of blocking the positive effects of others. While appropriate and credible policies are the basis for economic growth, they need to be backed by high-quality institutions, including ethical standards in corporate governance. Policymakers should build institutions in parallel with engaging in reforms and also ensure that institutions stay consistent with the requirements of a changing environment. However, given the diversity of institutional settings and the success of different economic strategies among G-20 countries, there is no single template for strong long-term growth. Policies need to be shaped to the special circumstances in individual countries. Efforts along these lines will unfold their full potential in a favourable international environment, in particular in the context of a robust and effective international financial and trade architecture which supports countries in the adoption of these principles.

Monetary and financial stability

- Price stability is indispensable for sustainable economic growth as it fosters investment and saving. Inflation is destabilizing and has a strong negative impact on the poor. Deflation squeezes profits, discourages investment and leads people to postpone spending. Experience has shown that central bank independence helps to achieve the goal of price stability in the long run.
- Fiscal discipline is equally important. Fiscal policy must ensure that public expenditures and debt remain at reasonable levels in relation to national aggregates in order to prevent economic growth being restrained by crowding-out, anticipated future tax increases and inflationary pressures. Public expenditure composition and the tax system should ensure fiscal sustainability without discouraging investment and employment. Demographic challenges may generate additional needs for consolidation and restructuring of public expenditure, including reforms to ensure the viability of public pension schemes. In addressing these challenges, transparent budget procedures are of the utmost importance.
- The domestic financial sector must be able to withstand economic shocks without giving rise to systemic problems which impair the allocation of savings to investment opportunities and the processing of payments in the economy. Excessive borrowing in foreign currencies for domestic activities has been identified as a major cause of international financial crises. Currency

mismatches could be diminished by strengthening domestic banking systems and capital markets. Strong domestic financial sectors can reduce the need for foreign currency borrowing and become an alternative channel of external funding by attracting foreign investors into domestic currency instruments. High priority must be given to implementing the relevant internationally recognised standards and codes.

- The liberalisation of the capital account yields essential efficiencies and benefits for economic growth. However, countries still opening their capital account should proceed prudently in order to avoid an excessive volatility of capital flows. A prudent approach would be based on sound macroeconomic policies and gradual deregulation of the domestic financial sector combined with adequate enhancements of the supervisory framework. The elimination of restrictions on capital movements should be appropriately sequenced. Experience has shown that countries seeking domestic monetary autonomy while substantially liberalising their capital account should increase the degree of exchange rate flexibility accordingly.

Enhancing domestic and international competition

- Competition is the driving force of economic growth because it fosters efficiency and stimulates innovation. It is also essential for strong investment activity. Carefully designed policies of deregulation, privatisation, and liberalisation of international transactions are important means of strengthening competition. However, ensuring competition and the functioning of markets requires setting the right incentives through efficient institutional arrangements. In particular, policymakers should aim at strengthening and enforcing intellectual and other property rights, contract law, bankruptcy procedures and anti-trust regulations. Also, efforts will be required to promote good governance and combat corruption.
- Global trade liberalisation is an essential instrument to promote growth by channelling resources to their most productive use. While trade liberalisation needs to take due account of adjustment costs, policymakers worldwide should move ahead vigorously on the basis of multilateral commitments. Multilaterally consistent bilateral and regional agreements can also contribute to trade liberalisation.
- Flexible labour market conditions are crucial cornerstones in achieving high employment levels and broad participation of the labour force. Both wage levels and working hours need to be responsive to market requirements and reflect national circumstances. Flexibility in work arrangements needs to be complemented by policies to provide opportunities and incentives to gain and improve skills, foster labour mobility, strengthen incentives to work in the formal sector and reduce information asymmetries.
- Small and medium sized enterprises (SMEs) are an important element of dynamic economies as they play a central role in creating jobs, facilitating the absorption and adaptation of technology and strengthening entrepreneurial skills. Policymakers can support SMEs by committing themselves to non-discriminatory measures and ensuring access to financial services, risk capital, innovation networks and public R&D programmes.
- A favourable overall investment climate, including adequate infrastructure, will support domestic capital accumulation and also be attractive for Foreign direct investment (FDI). FDI is generally a powerful means of enhancing competition and the growth potential. For one thing, FDI facilitates the international transfer of know-how, thus fostering the competitiveness of the host country directly. For another, FDI can help to improve the productivity of local companies by stimulating imitation of new technologies.

Empowering the people and reducing poverty

- Mobilising all productive forces of a society requires empowering individuals and enhancing economic participation. Equal economic opportunities allow people to better provide for themselves and their families, thus helping to reduce poverty and social tensions. Education and training are key requirements as they improve people's chances of finding jobs and contribute to higher productivity. The broadly-based provision of high-quality primary and secondary education should be a responsibility of governments and provides the basis for successful tertiary education. Raising the level of education contributes to the quality of governance as an educated population is better placed to demand the provision of good governance and sound institutions.
- Broadly-based access to a wide range of financial services and reducing impediments to small businesses, such as the time to start a business, is of crucial importance as it fosters entrepreneurial capacities and facilitates the integration of people into the formal economy.
- While employment is the first and best safeguard against social exclusion, social safety-nets are needed to cushion the effects of unemployment. Moreover, the elements of social infrastructures such as clean water, sanitation and basic health services are public goods whose provision has a positive impact on welfare and potential growth. It is important to design social policies so as to permit market mechanisms to function effectively.