

Interview with David Dodge, Governor of the Bank of Canada

Conducted by Candida Tamar Paltiel, G8 Research Group

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CT: We've already covered the historical aspect of the creation of the G20. Could you convey to us what your role is in the G20 group?

DD: The G20 is composed of central bank governors and ministers of finance. And there's good reason for that because its origin came because of financial instability and the fact that a number of Asian countries got into very severe difficulties during 1997 and 98, and then subsequently Russia. And the view was that at least a good part of the reason they got into difficulties was because their financial systems were not very robust. And so when we had a little bit of difficulty in the economy and then got magnified many times through the financial systems which were not as strong as they should be. And so both finance ministers and governors play a role because finance ministers deal with the general legal framework but it generally the central banks that are then charged with trying to make the thing work. Certainly it's the central banks that have to cooperate to try to deal with the problem with they arise. So we are sort of Mutt and Jeff, the central bankers and finance ministers. We each have our own role to play.

CTP: I was wondering how it works?

DD: Well, first let's start with people. The central bankers of all the countries that are involved are very sophisticated individuals and by and large even in the countries that have less sophisticated, less developed systems, the central banks and the staff of the

central banks really are very much tuned into the problems and knowledgeable about the problems. That's probably most true in China where the real locus of expertise is in dealing with finance is in the central bank rather than in the ministry. But as you go right across the countries whether it be Indonesia or South Africa a lot of expertise is there and we talk to each other very much on equal terms so it's not as difficult as one might think because a lot of our backgrounds are similar and certainly we understand the issues in a similar way.

CTP: Could you comment on your advisory role to the emerging economies?

You're right — we have developed in Canada or the United States or Australia or in Europe, we've developed pretty robust systems but they've been developed over a long period of time, and what we're trying to do for a number of the other countries is to try to telescope into a relatively short period of time develop that have taken place over a long period of time here. So one of the key things is of course technical help in moving things forward so we have the Toronto centre, for example, to try to help build stronger systems of banking supervision in the emerging market countries to train banking supervisors. It's really in that regard that we have our most important role to play.

CTP: How would the Anti-terrorism Action Plan work?

DD: That's quite interesting. The anti-terror action plan is a little different from the financial stability aspect because it is dealing across institutions that are not necessarily in the central banks. Many countries have charged an agency other than the central bank with the task of dealing with money laundering or with terrorist financing. That's true in

Canada and many, many countries. In that regard we play a much more supportive role as opposed to an active role whereas on the financial stability side, was what was the problem of the peso crisis of '95 or the Asian and Russian crisis of '97 and '98 we played a critical, central role.

CTP: How do you propose to deal with capital flows to emerging markets?

DD: Secretary O'Neill said basically capitalism is a coward and capital will always seek safe havens. If in fact we are going to have capital markets that really serve emerging markets well particularly in times of stress, then it's critical that those emerging markets be very robust and that the standards they follow are similar to the standards that are followed in the safe haven markets, which tend to be markets like the United States, Great Britain and Canada and so on. So a very important way of trying to deal with the problems of the emerging market countries is for them to build financial systems that are robust which meet standards that are demanded in financial centres in London, New York, Toronto and so on. And that's where we do come in. And so what one would hope is, each period of stress will see less of a widening-out in the interest rate differentials for the emerging markets and for the developed markets and that's what we're trying to do.

CTP: Was there any discussion of the Argentina crisis?

DD: There has been for a long period of time, a concern to try to find mechanisms to help countries to avoid that crisis. My experience goes back to Latin America in the early 1980s. What we did then was try to pick up the pieces after the fact. By the time we got

to the debt crisis of the 90s in Mexico and then Asia it was becoming clear that what we had to do was invest in an ounce of prevention rather than in a pound of cure.

There began to be a bit of a view that that should take place, but that view has been difficult to bring forward because we have tended to deal with these things on a one-off basis, so since each crisis has its own unique elements there were a number of countries, and indeed within the Fund, the view that you really had to deal with these on a one-off basis. There are two streams of thought and what has really happened over the last six or eight months is that through the efforts, in particular of Canada and the UK (the Bank of Canada and the Bank of England have been working jointly on this.) but others as well. What we have been trying to push forward is the prevention agenda and to find ways to involve the private sector earlier on, so that it wasn't always a bail-out from the IMF after the fact, but really to try to find mechanisms that would prevent the problems from arising in the first place and then secondly to establish rules of the game as to how problems would be dealt with in the event they arise, because you can never avoid them altogether.

CTP: Did these issues actually come up during this particular meeting?

DD: No, no in fact it's very important and that's where the G20 is actually being quite helpful because the Central Bank of Argentina, for example, and the Central Bank of Brazil and they have to live with these problems day in and day out and they're very important, and they're very competent folks. So they really add to the discussions and so I've witnessed over the course of 2001 some very real progress. Not that we have

concrete plans yet, don't get me wrong, but the consensus is building, that frameworks really need to be established and we can't do everything on an ad hoc basis.

CTP: What do you see as the challenges to globalization?

DD: Let me say that the breaking down of barriers to the exchange of goods and services and finance have really contributed tremendously to the economic growth over the period since the second World War. Now, initially, most of those barriers that were broken down, were broken down between the developed countries, the OECD countries. And one can see the tremendous growth in those countries that came because of expanding trade, because capital markets were liberalized over that period tremendously. It's hard to remember now, but as recently as the 1970s, some OECD countries had restrictions on capital flows. And so what we now assume as the norm in the OECD world is actually relatively new and we worked very hard in the OECD world in that period to break down those barriers. More recently let's move to a global basis involving not just the so-called rich OECD countries, but countries right around the world to try to bring the benefits of these open capital markets and these open trading systems. First we've seen the tremendous developments in Asia, a number of the southeast Asian nations that have come along from very closed economies to very open ones and the tremendous growth that it's brought. We have seen countries such as Chile move again in the same way over this period. Brazil... Argentina not quite so open yet. But we're all working hard to open that up. So those are the benefits. Now the risks that come as you tear down borders is that problems that emerge in one part of the world, then get transmitted very quickly to other parts of the world. And that is a very real risk, and so it becomes incumbent on us

to work with trading partners, with financial partners right around the world to avoid that problem. In some sense we were lucky at the time of the Asian crisis that it didn't go deeper because the United States was in such a strong period of growth, that despite the problems, it could absorb so much by way of imports that it was able to counteract almost single-handedly the potential implosion of countries such as Korea at that point in time. We're in a little trickier period now because we not only have this one very strong engine of the United States. Japan remains very weak as it has been since 1990 and Europe is going through a very important period which will build a much stronger Europe, but which involves a lot of concentration of the Europeans on its own internal system, in particular this year, on the building of a single currency. So there are many more dangers this time because we don't have that one very clear engine of growth, the United States, that we had in 1997/98 that pulled us through. So it is a real risk that as you open up, as you trade globally rather than locally, that something that happens in a far-off corner of the world will effect you. In fact, there are no far-off corners of the world anymore.

CTP: What kind of challenges to globalization do you see?

DD: Let me start by saying that relations between the treasuries have tended to be quite good even in times when one might have said the US, generally in terms of its foreign policies, was acting in a more unilateral manner. We talk the same language, we tend to understand the problems, I wouldn't say exactly the same way, but in a way that makes it perhaps a little easier for treasuries to deal with one another, whereas foreign ministries have sometimes more difficulty. I'm not blaming foreign ministries, I'm just saying that's what happens. That a [not clear] for central banks. Central banks really can talk to each

other through all sorts of differences, political and so on. And so it's hard for me to say I've noticed a real shift since February. Secretary O'Neill was new in February and every time there's a new player, the new player has to take a bit of time to establish his or herself. But generally speaking we have enjoyed through the central banks, and the treasuries around the world, good relations so it's probably much harder for us to detect a shift than if you were to ask John Manley, for example.

CTP: How do you address the knowledge gap between the G20 and what the public perceives?

DD: Let me speak from my own perspective as central banker first, and then more broadly in that regard, because getting information out, not just to protestors, but to the general public about what we're doing has always been quite difficult. I would say, if I compare the year 2000 with the year 1990 when I was Canada's G7 deputy, I would say that every country in the world is making a much greater effort now in getting information out. Transparency is the watchword in 2001 in a way that it was certainly not the watchword in 1991. So in terms of will to get the information out I would say there's been a tremendous advance over the last decade. The trouble is when you come to some of these financial dealings, there it is difficult technically to explain what we're doing. We've been trying to explain to Canadians how it is the Bank of Canada operates for the last decade – even very sophisticated people sometimes don't understand. So we're not maybe the greatest communicators in the world, but it's not for want of trying. And so I think there's always bound to be some difficulties with someone in a suit and tie trying to communicate with someone carrying a lunchbox or someone carrying a placard what

you're trying to do, and all you can do is work away at it over time. I think we have made some real progress over the last decade and I hope we'll make even more progress over the decade to come.

But one of the great things about the G20 is that what we're doing is working with the folks in some of the countries that are in more difficult shape, so that we are working together and it's very interesting to listen to my counterpart in India, Mr. Jalal, trying to explain why, to Indians, it's important to move some of these processes forward. None of us perhaps do this all that well, and it's hard to do, but all we can do is keep working at it, because the one thing I think is absolutely critical to understand, is the aims and objectives of what we are trying to do, which is to establish better growth to deal with some of the world's income distribution problems, and to raise the standards of living of people.

Those are our objectives every bit as much as they are the objectives of what you call the protestors. Certainly the protestors with goodwill who are out there just as in the days of civil rights, and the objectives of lawyers and people involved in justice were to try to push civil rights forward – the same agenda as protestors at the time (of which a number of us in our younger days were a part of that game). But when you're young, you're more impatient and you try to push the system, and that's fully legitimate and indeed, I hope, helpful.

CTP: What do you feel you have achieved here?

DD: First, let me say, I think Canadians ought to be really proud of what this country has done, certainly over the last five years in trying to push the agenda of opening up, and of inclusiveness of bringing the emerging market countries and the less developed countries into the decision-making process. We've been trying very hard to do that and I think step by step, slowly, I hope perceptively, been making progress in doing that. So I think Canadians really ought to be proud of the positions we've taken and of the people who work very hard to move this forward.

Now it is always incremental and what I think is probably... from a central bank perspective, from a financial perspective... what I think is very important over the last year, is that in large part... (we always are very modest as Canadians and sometimes maybe we should not be quite so modest)... we've been able to move the system a long way in understanding that prevention of crises is probably a lot better than picking up the pieces afterwards. We have certainly made considerable progress here in terms of establishing a framework for dealing with financial crises. For me as a central banker, that was terribly encouraging and I think it should be encouraging for all Canadians. But I think secondly, and critically, there was real progress made in the understanding that as we try to open the markets, we have to also assist those new players, and those players who are poor, to be able to participate in the markets as we open them. We can't just open them and say it's all up to you now. We also have to help them to have the tools that they need. I think that certainly around the G20 table and then subsequently at the IMFC meetings and the development committee meetings, I certainly had a much greater sense

that that agenda was moving forward. But it's slow. And this is an area where patience is important, and you just have to keep at it. And at it, and at it.

CTP: What do you see the agenda will be at the next G20 meeting?

DD: Certainly, we've been left with a lot of work to do coming out of this meeting, and if we don't make some progress on a financial framework that prevents crises over this next year, then we really won't have lived up to the hopes that were bred here. But I think we can. And I have to emphasize that it is hard work... it involves armies of lawyers and accountants and bank regulators, and market regulators, and so it's not something that just happens overnight, but I think we've made significant progress in setting the ground floor, and I hope by the time we meet next time we will be able to report very real progress.

Also, the one thing Sept 11 has made us realize is that we really are pretty interdependent and we do have to work with each other in a better way than we have in the past. And so what we've done here along with what was done in ...(unclear)... I think is really quite important. Now the real acid test is going to come when it runs up against the hard politics of the developed world – quotas on textiles, subsidies for agriculture, these sorts of things. This is going to be a bit of a prolonged struggle. And obviously as the world economy starts to improve (and by the way, we are little more optimistic than the IMF is on this) then it's much easier to make progress on some of these difficult structural issues.