G-20 fallout: Trade barriers, tensions could rise

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WASHINGTON (AP) — The world's most important economies are going home to look after themselves. They left their summit without any meaningful agreement, finding it ever harder to cooperate and more likely to erect trade barriers to protect their own interests.

The Group of 20 meeting of leading rich and developing nations ended Friday in South Korea with no solutions to longstanding tensions over trade and currency, and with the cooperation of the 2008 financial crisis now a distant memory.

The U.S. couldn't persuade other countries to pressure China to stop manipulating its currency or limit their own trade surpluses and deficits. The Americans faced charges of doing some currency manipulation of their own by pumping $600 billion into their economy.

The stalemate in Seoul means that trade disputes could intensify, warns Eswar Prasad, professor of trade policy at Cornell University. He's worried that there "may be more open conflicts on currency matters. This has the potential to feed into more explicit forms of protectionism, which could set back the global recovery."

The summit was a diplomatic setback for the United States.

China was supposed to be the villain of the G-20 meeting. The U.S. and other countries have accused Beijing of keeping its currency, the yuan, artificially low to give its exporters an unfair advantage. The currency manipulation helps Chinese exporters by making their goods less expensive around the world, leading to charges that cheap Chinese products cost America jobs at a time when U.S. unemployment is stuck at 9.6 percent.

The U.S. wanted to rally other G-20 delegates to strong-arm China over the yuan. A stronger yuan would reduce the U.S. trade deficit with China, which is on track to match the 2008 record of $268 billion. But the U.S. argument was undercut by accusations that the Federal Reserve was rigging the currency market itself.

Last week, the Fed said it would essentially print $600 billion to jolt the U.S. economy back to life. The Fed says its plan to buy Treasury bonds was designed to lower long-term interest rates, spur economic growth and create jobs. Since the Fed hinted at the policy in late August, the Dow Jones industrials have risen 13 percent , and interest rates on 30-year fixed-rate mortgages have hit a record low of 4.17 percent.

But foreigners saw a more sinister intent: to flood world markets with dollars, driving down the value of the U.S. currency and giving U.S. exporters a price edge.

"Basically, what happened was a diplomatic coup for China," says William Cline, senior fellow with the Peterson Institute for International Economics. A few months ago, countries from Brazil to Germany were criticizing Chinese trade policies. "Fast-forward, and now China and Germany and Brazil are blaming the United States for causing currency problems."

Emerging economies also complained that the Fed's bond purchases would push Treasury yields so low that investors seeking higher returns will overwhelm their fragile markets. The fear: Investors would sink money into emerging market assets — currencies, stocks and other investments. That would push up their currencies, hurt their exporters, trigger inflation, create bubbles in stocks and other assets and leave them vulnerable to a crash when investors withdraw their money.

The final G-20 statement Friday endorsed the idea that emerging markets can protect themselves from the threat of such "hot money" by imposing controls on the flow of capital — a measure that used to be considered "a big no-no" and a violation of free-trade principles, says Homi Kharas, a senior fellow at the Brookings Institution. The trend is already starting. China and Taiwan this week announced new capital controls.

The fear is that countries will take even stronger steps to give themselves an advantage, creating the risk of a currency or trade war. The U.S. House has already passed legislation that would let the U.S. government impose punitive tariffs on Chinese imports in retaliation for the weak yuan, though the Senate has not followed.

Cornell's Prasad expects to see China and other countries impose tariffs and duties, subsidize their exporters with cheap bank financing or tax credits, bring cases against each in the World Trade Organization and use bogus health concerns to block some imports.

In a sign of the United States' diminished clout at the summit, the U.S. could not even close a long-awaited free-trade agreement with close ally and summit host South Korea. The trade pact would slash tariffs and other trade barriers between the two countries.

As the G-20 meeting closed, President Barack Obama and many other leaders flew to Japan for the Asia-Pacific Economic Cooperation summit in Yokohama, Japan, on Saturday and Sunday.

At the height of the financial crisis in 2008 and 2009, the G-20 nations tried to present a united front, agreeing to take steps to boost their economies, to reform their financial systems and to

Canadian Prime Minister Stephen Harper, right, and President Barack Obama walk onto the stage with South Korean President Lee Myung-bak at the Small Medium Enterprise Finance Challenge Award Ceremony at the G20 Summit in Seoul, Korea Friday Nov. 12, 2010. (AP Photo/The Canadian Press, Adrian Wyld)

Map

reject protectionist policies. But now that the world economy is growing again — and China and other emerging markets are booming — "that unity has begun to dissolve," Prasad says. "The group is now splintering with competitive policies taking the place of coordinated policy actions." The result: "a situation ripe for conflict."

The G-20 itself acknowledged the problem in its final statement: "Uneven growth and widening imbalances are fueling the temptation to diverge from global solutions into uncoordinated actions." But the go-it-alone approach, the statement concluded, "will only lead to worse outcomes for all."

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