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## Worth the hype? The effect of G20 summits on global financial markets<sup>☆</sup>



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### ABSTRACT

In the wake of the global financial crisis, the G20 has become the most important forum of global governance and cooperation, largely replacing the once powerful G7. Against this background, this paper looks at G20 meetings at Ministerial and Leaders level to see whether they had an impact on global financial markets. To assess their impact we run an event study and we look at equity returns, bond yields and measures of market risk such as implied volatility, skewness and kurtosis between 2007 and 2013. Our main finding is that G20 summits have not had a strong, consistent and durable effect on any of the markets that we consider, suggesting that the information and decision content of G20 summits is of limited relevance for market participants.

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## 1. Introduction

The 2007–09 global financial crisis has brought about a fundamental shift in global economic governance. The Group of 20 (henceforth G20) took the reins of the world economy from the G7. Indeed, the G20 came into prominence only after the Pittsburgh summit in September 2009, though the political consensus was already forged at the London summit in April, even it was established in the

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late 1990s.<sup>1</sup> This shift has undoubtedly brought a number of important benefits. Most important, global governance has become more broadly based and legitimate, with key emerging markets being represented and contributing to decisions at the global level. Nevertheless, doubts still linger on the legitimacy and effectiveness of the G20, which has received its fair share of criticism (“divided, ineffective and illegitimate”; Rachman, 2010).

Generally speaking, any global governance system faces an unavoidable trade-off between *efficiency* and *legitimacy*. On the one hand, a larger group is usually slower in taking decisions. On the other hand, the presence of more players makes it more legitimate. A relevant question is whether the current composition of the G20 is the best way to manage this trade-off, being aware that an ideal composition is probably unattainable (Carin et al., 2010).

Moreover, the question of legitimacy is also not straightforward, since one can distinguish at least between “input” legitimacy (the country composition) and “output” legitimacy (the outcomes stemming from G20 processes, irrespective of who takes the decision). In terms of the former definition, several observers have noted that the G20 composition is not clear and transparent (Vestergaard, 2011). Indeed, its current composition is based on criteria largely decided by the G7 and it has been influenced by US strategic interests. As a result, its composition is inconsistent. For example, it is not clear why countries such as Argentina and Saudi Arabia are members of the G20, while Spain is not, although Spain has an unclear status as a “permanent guest”. The lack of a clear input legitimacy implies that decisions in the G20 can be taken only by consensus, leading to too timid and hence suboptimal decisions. To solve this issue Vestergaard (2011) proposes to create a Global Economic Council in place of the G20, embedded in the institutional framework of the Bretton Woods institutions.

Turning to output legitimacy, the common opinion is that the record is mixed (Truman, 2011), being positive in some areas (catalyst for global financial regulation, management of capital flows) and poor in others (e.g., surveillance of the global economy). In this regard, Larionova (2011) notes that the G20 is still significantly less effective than the G8 in terms of accountability and delivery. Moreover, Angeloni and Pisany-Ferry (2011) note that G20 actions were effective at the peak of the crisis, when all countries had consistent policy objectives and priorities, but not when priorities started to diverge thereafter. Other observers have also emphasised the need for the G20 to become more accountable (Subacchi and Pickford, 2011).<sup>2</sup> Finally, another set of issues concerns the role of the IMF as the operational arm of the G20.

Against this background, the main purpose of this paper is to evaluate the G20 from a somewhat different, but in our view related, angle. We want to test whether G20 summits have been influential for global financial markets. Clearly, it is not the stated objective of the G20 to steer global financial markets, especially in the short term. Therefore, its impact on financial markets should not be seen as a yardstick against which the output legitimacy of the G20 should be measured. Nevertheless, financial market reactions to the G20 meetings still constitute a useful indicator of the information and hence decision content of G20 summits. If the G20 summits contribute to reaching agreement on key decisions, surely a consensus represents important news for financial markets. Indeed, we expect that an agreement reached in the premier forum for international economic cooperation should be reflected in changes in market prices and volatilities. Otherwise, G20 summits could simply be an effective way for Leaders and Ministers to get to know each other better, which facilitates cooperation later and on an ongoing basis. This would make G20 summits possibly still valuable, but it would not justify the media attention that they sometimes receive. In short, our analysis is aimed at achieving a better understanding of the nature of G20 summits. Our paper does not aim to give an overall view about the usefulness and role of the G20 in the field of international economic policy cooperation) more broadly.<sup>3</sup>

<sup>1</sup> The G20 has been established as a group of finance ministers and central bank governors in 1999 in the wake of the Asian crisis.

<sup>2</sup> The lack of a permanent secretariat is widely seen as a problem in the assessment of, and follow up to, G20 commitments.

<sup>3</sup> See also the debate on the Economist blog, e.g. the positions of Ricardo Caballero (“[G20 summits are] probably worth having but not much surplus is left after the travel expenses are paid for. The unreasonable part is the hype around these meetings. The G20 gathering is just a nice photo and venting opportunity; the speeches and debates are totally predictable (and boring).”) and Viral Acharya (“G20 summits are worth having. While the process of international dialogue and cooperation does not always yield tangible effective results, the counterfactual could be far worse. And the debates at the G20 do shape national agendas on various policies relating to trade, exchange rates, and financial sector regulation.”).

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