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The G20 and Global Capital Markets
Critical Issues and Analysis

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Introduction

October was a tumultuous month. It began with U.S. treasury secretary Tim Geithner testifying before Congress that the expected losses from the Troubled Assets Relief Program (TARP), which ended on October 3, would not exceed $50 billion. Analysts have estimated that two thirds of the $387 billion (of a possible $700 billion) that was loaned out has been repaid and that the Treasury has already made $25 billion in profit. Part of the profit comes from the sale of Citigroup stock, underway since the spring, with AIG and General Motors stock sales soon to follow.

In France, unions and their supporters took to the streets in protest to the government's plans to raise the retirement age from 60 to 62 and the full pension age from 65 to 67. By the end of the month, the protests had subsided with the passage of the bill and fear of losing public support if they continued.

The International Monetary Fund (IMF) reported in its semi-annual *Global Financial Stability Report* that the global financial system is still in a period of significant uncertainty and remains the Achilles heel of the economic recovery. Conditions in the global financial system now have the potential of jumping rapidly from benign to crisis mode. In major economies, deficits would increase despite efforts to the contrary and the real estate sector is prone to a double dip. The world economy will expand overall by 4.8% this year and 4.2% in 2011.

At the beginning of October, Jérôme Kerviel, the ex-futures trader with Société Générale who lost billions for the investment firm and brought it to the brink of collapse, received a five-year sentence with two years' suspended and was ordered to repay the €4.9 billion he lost in his risky bets. The ruling, one of the harshest in history, is being appealed. The ruling also had no impact on volumes in the U.S. equity markets, which declined by more than 20% in both August and September and a full 40% since the flash crash in May. Investors are weary and are sitting on the sidelines. They are also waiting to see the outcome of the midterm election in November and what the new rules are going to be under the Dodd-Frank Bill.

Around the world, interest rates remained largely unchanged with the exception of Japan. Japan returned to its zero rate policy by lowering its interest rate to 0-0.1% and announced it would purchase assets worth ¥5 trillion. After three consecutive rate hikes since June, Canada left its rate at 1%. The Bank of England left its rate at 0.5% and maintained its asset repurchase program at £200 billion. The European Central Bank (ECB) left its rate at 1%. Both Norway and Sweden will likely leave their rates unchanged well into next year because of internationally low interest rates. Fitch downgraded Ireland because of the rapidly increasing cost of recapitalizing its banks, which has reached €45 billion.

At the final meeting of the European task force to improve economic governance and safeguard the euro in mid October, France and Germany struck a deal to reopen EU treaties to reform the eurozone's budget rules after the sovereign debt crisis that had threatened to topple the euro in the spring. To reopen the treaties would require agreement from all 27 members, and views currently differ on how to deal with wayward member states. Later in the month, all members agreed to a permanent bailout fund for the eurozone members unable to attract private financing as the temporary European Financial Stability Facility, set up during the sovereign crisis, will cease operating in 2013.

In the midst of all this, the G20 finance ministers and central bank governors met on October 22-23 in Korea with little progress on the issues of exchange rates and rebalancing but came to resounding conclusions on the reform of the IMF to make it a more resilient and legitimate institution. Ahead of next month's G20 summit in Seoul, international organizations were busy preparing their final reports to meet the deadlines set for them in Toronto in June.