Rapporteur's Report[1]

THE IMPACT OF CHANGES IN THE INTERNATIONAL FINANCIAL SYSTEM ON RUSSIA, CHINA, THE UNITED STATES AND EUROPE

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The latest international symposium organized by the Financial Services Volunteer Corps (FSVC), funded in part by Carnegie Corporation of New York, took place in St. Petersburg, Russia, during June 30-July 2, 2019. The symposium brought together 25 leading experts from Russia, China, the United States and Europe to discuss topics related to the state of the international financial system. These topics included the impact of financial and economic issues on foreign policy, the financial and economic engagement of advanced economies with the emerging market world, and the risks and opportunities presented by new financial technologies.

The FSVC/Carnegie symposia have taken place annually since the start of the new millennium. A core concept underlying them has been that the most intractable problems confronting the world today will require multilateral coordination among key countries if they are to be successfully addressed. These complex problems do not fit neatly into the silos of individual expertise, and thus demand broad-based collaboration and earnest communication among experts and policymakers alike.

The global financial system lies at the center of many of the world's greatest challenges, as well as the most promising opportunities for collaboration. A key drive behind this year's discussions was therefore to understand how recent developments and rising trends in the international financial system are impacting, and will continue to impact, relations among Russia, China and the U.S., and identify potential areas of mutual interest in tackling shared financial sector issues.

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[1] This Rapporteur's Report was prepared by Charles Brahaney. The Principal Investigators for the project are Harry Harding and J. Andrew Spindler. Harry Harding is a University Professor and Professor of Public Policy at the Frank Batten School of Leadership and Public Policy, and Senior Fellow at the Miller Center of Public Affairs at the University of Virginia; and Yushan Scholar and Adjunct Chair Professor at the College of Social Sciences of National Chengchi University in Taipei. J. Andrew Spindler is the President & CEO of FSVC. A list of participants in the symposium is provided in the attached annex.

FSVC is a not-for-profit organization whose mission is to help build sound financial sectors to support healthy market-oriented economies in developing and emerging market countries. Additional information about FSVC can be found at www.fsvc.org.

Opening Remarks

With these objectives in mind, the Principal Investigators of the symposium offered opening remarks to participants. They first expressed their gratitude to Carnegie Corporation of New York for making this series of symposia possible. They noted that we stand at a moment of tremendous change in the world. This moment is akin to post-World War II reconstruction or the collapse of the Union of Soviet Socialist Republics (USSR) in magnitude, but more obscure in causation. Climate change, the shifting nature of globalization, innovations in communications and financial technology, and the use of big data in business, economics and politics all represent irrepressible challenges that, as they come to fruition, make this moment in history highly volatile. New governing challenges, such as the fracturing of nation-states, the European Union under tremendous stress and the spread of new and extremist ideas, compound the notion that we stand at an inflection point in world history.

In terms of the international economy, Russia and China are both struggling to escape the middle income trap, or the difficulty of finding new sources of growth and dynamism. Russia briefly reached high-income status according to the World Bank, but then lost it due to Western sanctions, the global energy crisis and domestic obstacles to reforming the Russian economy in ways that would allow the export of higher-value goods and services. China, on the other hand, continues to grow more steadily despite its current economic downturn, and has moved into upper-middle income status. China is now struggling, however, to make the final leap into the high-income category, in part due to resurgent American protectionism, but also because of domestic obstacles to structural supply-side reform and weighty corporate debt. For their part, the U.S. and Europe suffer from the high-income "treadmill", whereby their economies must strain to maintain high enough growth rates just to keep their current status in the global economy. They are weighed down by demographic changes, the burdens of overgrown or inefficient welfare states, and rising government debt.

These economic dynamics have led to domestic populist backlashes to globalization, which are reflected differently in each country. On the one hand, many middle-income countries face "revolutions of rising expectations", whereby populations demand continued strong economic growth. On the other hand, high-income countries face "revolutions of declining expectations". Some of the middle class in these countries has taken on anti-immigration sentiments, protesting established elites who they claim have neglected their interests. Over the past 30 years, the middle class in advanced economies has experienced significantly less growth than the upper classes. Youth unemployment and poorer job prospects exacerbate this unrest.

Internationally, the idea that economic interdependence both demands and reinforces cooperation is quickly fraying. As the global economy stands today, interdependence seems to have created more rivalry than cooperation, and the resulting strain has prompted the early stages of decoupling between the U.S. and China, in particular. The increased use of sanctions and other coercive foreign economic policy tools, which have played a central role in souring the current geopolitical atmosphere and prompting decoupling, some suggest, may also spur a new international arms race.

Session I – Current Relations Among Russia, China, the U.S. and Europe

In looking at current relations among these key powers, some participants noted that the most significant driver of security relationships today is economics: finding markets for products, or undermining the ability of others to do so. Geostrategic competition appears to be morphing into geo-economic competition. The Arctic region is a forward-looking example. China eyes it as space for infrastructure and trade routes, Russia looks at it for resources and trade routes, and the U.S. seems to have few grand designs other than to monopolize and block access to the region. Competition will be fierce in coming years.

U.S.-Russia Relations

The U.S. and Russia have numerous areas of overlapping interest. Nuclear stability, rules of engagement on cybersecurity, non-interference and regional conflicts, and energy security are some of them. Thornier issues include Ukraine and Crimea, Syria and Venezuela, the U.S. sanctions regime against Russia and election meddling. The U.S.' current domestic political sentiment toward Russia is overall negative. The Trump administration made early overtures to Russia but has since backed away due to domestic political pressure from both the Democratic and Republican parties.

U.S.-China Relations

Technological piracy, suspicions about China's Belt and Road Initiative (BRI), geopolitical tensions involving the South China Sea, Taiwan and the Korean Peninsula, currency manipulation and tariffs possibly escalating toward a trade war are all points of friction in the U.S.-China relationship today. The U.S. grand strategy of bringing China into the liberal international order in the hope that China would evolve toward a liberal democracy has been proven ineffective thus far. One participant observed that the U.S. still wants China to be a different country than it is. China's government will realistically, for example, continue to fund technological development. With regard to trade tensions and each country's position in the global economy, participants noted that many of the underlying tensions between both countries may be a result of an imbalance in the global allocation of real wealth.

Decoupling

The tensions between the U.S. and China have initiated an economic decoupling of the two countries. Many U.S. firms have begun shifting supply chains out of China to other East Asian countries, and most of these companies may not return to China soon, even if trade tensions subside in the next few years, because they do not want to get caught up in a conflict again. Most worryingly, the decoupling trend appears to be happening across a large number of sectors. Huawei has announced that it has found substitute suppliers for imports from the U.S. to ensure cheap, unrestricted access to necessary input materials and technologies, regardless of trade tensions with the U.S. At the same time, it seemed unlikely to one participant that smaller Southeast Asian countries will be able to handle the complete rechanneling of American supply chains through their factories and shipping ports. A number of U.S. industries, including the military, also rely on certain Chinese technologies.

China-Russia Relations

Russia's ability to continue to play a major role on the international stage depends at least in part on its continued good relations with China. There was general debate among participants about the strength of the Russia-China relationship going forward, and whether its positive prospects today are overly reliant on the warm personal relationship between Presidents Putin and Xi.

The two leaders' relationship has helped spur a series of mutual policy agreements and favorable economic ties. In a joint statement this June, they reaffirmed their commitment to the foundational principles of the 2001 Treaty of Good-Neighborliness and Friendly Cooperation. There are also other impersonal factors that will continue to keep the relationship stable. Most importantly, Russia and China both seek a multipolar world order as an alternative to the U.S.-led liberal international system. Reforming international governance and financial institutions so that non-Western powers have far greater representation is a priority for both countries, and a major shift in the Russia-China relationship is therefore unlikely until fundamental geopolitical realities change. At the G20 summit, for example, one theme brought up by Russia and China was the use of national currencies in bilateral transactions.

Another area of common interest is prosperity in Eurasia. The BRI and the Shanghai Cooperation Organisation are two platforms for building broader integration in the Eurasian continental region. Russia is expected to further advance the latter project at the Brazil, Russia, India and China (BRIC) Plus summit next year, China having introduced it this year. It is also likely that Russia-China collaboration will grow in the area of technological development.

At the same time, one participant noted that China is generally compliant with U.S. sanctions legislation. Russian companies have faced significant challenges in financial compliance with Chinese banks because of this. Therefore, there are limits to China's capacity and willingness to act as a "black knight" for Russia.

Relations with the European Union

The European Union's economy is moderately healthy, and there seem to be fairly broad pro-E.U. sentiments among E.U. citizens, outside of strong nationalist tides in countries such as Hungary and Italy. The primary challenge for the European Union is a lack of vision and leadership against the current backdrop of identity politics, migration pressures and Brexit negotiations.

The withdrawal of the U.S. from the "Iran Deal" and the Paris Climate Agreement, and its tariff threats and NATO bargaining are points of friction with the European Union. And yet, some participants argued that much of the tension between the U.S. and the European Union is more rhetorical than substantive. Worryingly, however, the E.U. public appears to be becoming more anti-American, and perhaps even slightly pro-Russian.

Demographics

Finally, current and projected demographic trends will have a significant impact on the relations among the key powers. Demographics are an oft overlooked but nonetheless foundational component of the global economy. Demographic and human capital accumulation trends are fairly good indicators of the future economic impact of a country or region. As most advanced countries have demonstrated in recent decades, declining fertility rates tend to be extraordinarily difficult to reverse. Thus, a declining fertility rate may be better categorized as a "condition" – a situation that must be mitigated or adapted to – rather than a "problem" that can be solved. For advanced countries, there will likely be friction between demographic trends and economic expectations going forward.

Russia and China also face declining fertility rates and working age populations through 2040. Whereas the U.S. has traditionally benefited from relatively large immigration flows (although the trend has been reversed under the Trump administration), China and other Asian societies have not.

According to projections by the United Nations, Africa is the only continent that will experience sustained high birthrates and continue to grow. The considerable risk surrounding this development is whether or not the expanding youth and working age populations can be educated and then absorbed into growing economies and prosperous societies in Africa. Large immigrant tides could cause social and economic strain on host countries. Demographic-caused frictions could be eased if productivity and innovation can be boosted, and if nations can cooperate to create and distribute broadly more real wealth in the world.

Session II – The Current State of the Global Financial System

Overall, participants noted that the primary narrative of the past 30 years has been the integration of Russia and China into the global economy. The U.S.-led liberal economic order helped fuel China's growth. Russia has benefited as well, but not to the same degree. When Russia joined the international financial system in the 1990s – a system that emphasized transparency and free flows of capital – it left Russia more vulnerable.

Today, the situation is different. Official U.S. policy is hardly welcoming China and Russia into the financial world order. The U.S. government is increasingly using the hard tools of economic statecraft and neglecting its role in maintaining the rules-based foundations of the liberal world order. It is also true, however, that American hardline actions have not been implemented in a vacuum. Russia and China have both engaged in behavior that has provoked some of these responses. Unfortunately, many participants agreed that the damage caused by the heavy use of hard tools of economic statecraft may be quite long term, and difficult to reverse by a change in American leadership.

Participants then shared several observations about the current state of key financial systems, including those of China and the U.S.

The Chinese Financial System

One important measure taken by the Chinese government recently has been to start a new capital market that allows enterprises to apply for Initial Public Offerings (IPOs). This "STAR market" is similar to the U.S.' NASDAQ, though it is designed more specifically for tech innovation enterprises with research and development potential. Significant progress has also been made on the market pricing of companies' share prices. While China used to set a fixed price for stocks, if a company now wants to be listed on the tech board, its stock price will be decided by the market. This new market system is signaling a new policy aimed at attracting social funding for technology enterprises in all stages (startups to mature companies). These developments are spurred in part by a fear that, if the trade war with the U.S. escalates, it may dismantle the global value chain and increase systemic risk in the global financial system. China is therefore attempting to reduce its dependence on core technologies from the U.S. The country's efforts have already yielded early positive results: since late March 2019, 140 applications for IPOs have been accepted.

China has also begun to rework its policy of managing corporate debt. From a credit perspective, a situation was created wherein heavily-indebted private enterprises could not repay loans due to bad credit and their inability to obtain new "rollover" loans. As a result, private enterprises went bankrupt. Oftentimes, corporate default is treated as a regulatory failure; however, the government is avoiding drastic actions in favor of a more gradual approach. China has now slowed down de-leveraging at the corporate level and created more opportunities to raise direct financing through capital markets.

The U.S. Financial System

The regulated sector of the U.S. financial system arguably has a stronger financial foundation that ever before. Major U.S. financial institutions have over twice the capital that they had before 2007, and significant capital cushioning beyond the required amount. On the other hand, the U.S. has had ten years of zero effective interest rates, and one consequence is that the U.S. has seen several financial bubbles with dramatic and widespread impact. Today, the IPOs of companies like Lyft and Uber resulted in high valuations without the requirement of solid profits. Importantly, there has yet to be a serious deflation of financial assets, a risk today if the bubble bursts.

In terms of financial inclusion, over 20% of American households remain un- or underbanked. The expensive regulatory structure around financial institutions makes it hard to provide services to that population, and more efforts need to be made to address this need. FinTech companies are contributing to these efforts but, critically, many of these companies (e.g., Lending Club, SoFi) have yet to go through a financial crisis and be tested under serious strain. They also operate with very little capital, making them highly vulnerable. Furthermore, compared to the traditional financial sector, which has built trust over time (for example, via deposit insurance), the growing FinTech sector has not yet attained the same level of trust from the general public.

In addition to sharing insights about the Chinese and U.S. financial systems, participants also noted overarching trends in the global financial system, including the urgency of needed action on cybersecurity, the question of the continued dominance of the U.S. dollar and the growing importance of regional schemes.

Cybersecurity

Cybersecurity is a major concern of global financial institutions and countries alike, and there is an urgent need for the international community to cooperate and establish guidelines around cybersecurity and how to deal cooperatively with cyber risk. Some progress has recently been made in this area. For example, in 2018, a baseline for cyber examinations was developed, including a standardized set of compliance regulations and cyber assessment tools. This has enabled regulators and companies to focus on key areas to meet set standards. Creating effective cyber risk management strategies is also critical. One useful idea is the design and execution of threat exercise scenarios that allow participants to implement common approaches to after-action items from the exercise. There should also be an international taxonomy that is broader than highly-technical cyber terminology so that both public and private decision-makers can understand them. This will require the development of a neutral language that promotes discussions on multiple levels: public-private, U.S.-China, and so forth.

Dominance of US Dollar

In discussing the global financial system, the question was raised by some participants as to why it continues to depend on the U.S. dollar when that structure gives the U.S. a dominant position in the system. For several participants, the current system is an artefact of policy, politics and currency, reflecting the early postwar period when the modern global financial system was originally founded. With recent advances in information technology, some wondered why is it not possible to design a new system without anyone's currency playing a central role. Some countries are in fact seeking alternatives to the U.S. dollar. For example, in

2015, Russia created the MIR payment system in response to U.S. sanctions and fears that it could be shut out of global payment systems. China and many other countries have pursued the development of similar alternatives for the same reasons.

Regional Schemes

Finally, a participant noted that, increasingly, economic liberalization is emanating from regional schemes. The global sum of regional financing arrangements, which can be understood as regional International Monetary Funds (or IMFs), is now greater than the resources of the IMF. The sum of resources at regional development banks (e.g., the Asian Development Bank) is also several times larger than the resources of the World Bank. Despite the important scale of these regional schemes, there is hardly any regulation or coordination among regional development institutions, and they are not well integrated with global institutions. "Syndicated regionalism", or the horizontal coordination between regional systems on a systematic rather than ad hoc basis, could strengthen governance. The creation of a "Regional 20" (or "R20") based on the G20 could also strengthen coordination of regional financial arrangements and among regional development banks. This coordination could result, for example, in the pooling of the resources of development banks to finance megaprojects.

Session III – The Impact of Financial and Economic Issues on the Foreign Policies of Russia, China, the U.S. and Europe

Overall, participants noted that the U.S.' current foreign policy is fractured and incoherent. Many of the actions of the U.S. abroad seem to be driven by particular individuals in the inner circle of President Trump. Concern for domestic constituencies also seems to drive many of President Trump's decisions internationally. U.S. foreign policy therefore no longer seems driven by a fundamental American vision, as it was after the Second World War with its doctrine of "Enlightened Self-Interest". Participants generally agreed that the U.S. is taking actions now that are weakening the country's long-term interests. For example, the U.S. withdrawal from arms control treaties was deemed ill-advised and dangerous. Russia and China, by contrast, are both well-positioned to carry out more coherent foreign policies. Long-term strategic interests appear to guide Russian and Chinese foreign policy, though both countries also have domestic factors weighing on them.

Three key trends were further noted by participants during this session: the continued rise of populism, the use of sanctions and the possibility of a cryptocurrency replacing the U.S. dollar as the global reserve currency (due to the current hardline foreign policy of the U.S.).

Populism

Participants noted that, on both ends of the U.S. political spectrum, there have been critical failures in reasoning. One consequence of the broad-based liberal hegemony and free markets of the past three decades has been a rise in nationalist radicalization, as many

Americans have felt left behind. Unilateralists now agitate for an "America First" doctrine, but the resulting actions are weakening the long-term position of the U.S. The U.S. government must take into account these dynamics, which social media platforms have also fueled in part. Platforms such as Facebook, WeChat, WhatsApp and Instagram now represent one of the largest populations in the world today, and must be considered by the U.S. government and others when designing future policies and strategies for the dissemination of ideas.

Sanctions

Another key topic discussed was the increased use of sanctions. Several participants noted that the use of sanctions to coerce governments to change their policies is historically ineffective. In Iran, for example, U.S. sanctions aim to make it physically impossible for Iran to gain access to any money and technology needed to take actions that the U.S. does not approve of. This was deemed to be a shortsighted strategy. Another argument is that the U.S. aims to use sanctions to make the people of Iran sufficiently unhappy as to overthrow their government. Data on public opinion suggest sanctions are having the opposite effect, however.

Participants further observed that, if sanctions aim to promote compliance with rules, any alternative must first focus on making the rules better so that countries feel they have a say in developing the rules rather than having them imposed by outsiders. This approach would enable the international system to handle the violation of rules primarily through compliance management and diplomatic means, unless faced with egregious violations.

Cryptocurrency as Global Reserve Currency

Finally, participants were split as to whether a cryptocurrency will replace the U.S. dollar as the global reserve currency. Most participants agreed that the U.S. dollar will maintain its reserve position in the medium term at least, noting that something must stand behind a currency. What stands behind the U.S. dollar is the American economy, which remains the largest in the world. Wealth is being generated in the U.S. by its massive hub of technological and social network stocks. China may be the only country with the capacity to replace the U.S. in this regard. A smaller number of participants were more optimistic about the rise of a cryptocurrency as the global reserve currency in the next 20 years, noting the appeal of Bitcoin's decentralization, for example.

Most participants overall agreed, however, that the erosion of the U.S. dollar is highly probable. Hardline U.S. foreign policies are damaging the dollar's reputation as a convenient, liquid and readily-available currency, despite the fact that the U.S. dollar's share in international foreign exchange transactions has actually been increasing. One participant suggested that a softer alternative to dollar dominance could be the development of a multi-currency reserve basket. This would require the strong coordination of monetary policies, however, which would be challenging in the current international political and economic environment.

Session IV – The Financial and Economic Engagement of Russia, China, the U.S. and Europe with the Emerging Market World

Over the past four years, "de-risking" has become a major trend severely affecting emerging market countries. "De-risking" can be defined as the reluctance of large international banks to maintain correspondent accounts with banks in these countries. While U.S. financial institutions have not entirely withdrawn from emerging market countries, they have led the pull-back. Banks fear being caught in violation of sanctions and comprehensive anti-money laundering/combating the financing of terrorism (AML/CFT) regulations. As a result, correspondent banking relationships and dollar clearing services are much more difficult to acquire in emerging market countries.

The Perspective of Banks

Fear of regulatory action is clearly inhibiting banks in both the U.S. and Europe from engaging more with the emerging market world. From the perspective of many European banks, global financial institutions are over-regulated. Decisions seem to be made no longer purely on the basis of rational economic decision-making, but also on the basis of regulatory fears. In addition, there is a sentiment in Europe that U.S. authorities are not even-handed in their fines and prosecutions. Cyber risk is another key area of concern for major banks. Banks face cyberattacks on a daily basis, and the amount of technological resources dedicated to fending off such attacks has increased dramatically in recent years.

The Foreign Investment Outlook of China

Unlike the U.S., China has committed to large-scale economic engagement with emerging market countries. Two of China's goals appear to be attaining "Major Power" status by becoming an integral part of the financial and educational networks of developing countries, and securing raw materials and strategic positions in key countries. To achieve these goals, China is financing and executing large infrastructure projects, particularly in Southeast Asia, which China hopes to integrate into its sphere of influence in the long term.

To date, the results that China has achieved have been mixed. Deals to build railroads, ports and airports have involved tremendous amounts of debt that can quickly become onerous for developing countries. If a country defaults, China often assumes control over the project or some strategic collateral written into the initial agreement. For example, the loan agreement to build the new railroad between Nairobi and Mombasa in Kenya apparently included the port of Mombasa as collateral. If Kenya defaults, the port of Mombasa would be placed under Chinese management and control. Moreover, China appears to care little about corruption in the countries in which it invests, thereby providing a known supplier for corrupt governments wanting to develop infrastructure. Overall, China's investments do not appear to have engendered a lot of influence and goodwill abroad, or at least not as much as should be possible with this kind of development work.

U.S. Response

Overall, many participants agreed that the U.S. currently has limited capacity to respond to China's investment in emerging market countries. The Trump administration has increased its allocation of funds for development projects, but not nearly to the scale required to compete effectively. There has also been tremendous pressure from the U.S. Treasury Department to shift the focus of U.S. investment from infrastructure projects to macro-economic policy and civil society development. Large infrastructure projects have been deemed ripe for corruption, and the American business community does not want to be found in violation of the Foreign Corrupt Practices Act. Moreover, the U.S. structure for investments emphasizes joint private-public funding. This is problematic as raising private sector funds for large-scale infrastructure projects requires long timeframes for completing the projects and achieving a satisfactory return on investments. Finally, some participants agreed that the U.S. has lost much of its infrastructure knowledge, as experts have either retired or moved to other countries.

The Financial Action Task Force

While the Chinese foreign investment model has focused largely on the BRI and infrastructure investment, several participants emphasized that effective economic development must also include the development of market institutions and trust. In that regard, the Financial Action Task Force (FATF) process could be an important part of the solution for establishing compliance standards for foreign investments. FATF conducts periodic reviews of the AML/CFT compliance frameworks of countries, including Russia, China and the U.S. The institution has strong credibility: if a country fails to meet FATF standards and is placed on its watch list, foreign investments tend to decrease. Moreover, as of July 1, 2019, the presidency of FATF has rotated from the U.S. to China. This changing of the guard offers a real opportunity to tackle corruption in emerging market countries through greater cooperation among key FATF members such as Russia, China and the U.S. If such multilateral efforts were proven effective, they could promote flows from the global private sector to countries that meet FATF standards.

Session V – The Implications of New Financial Technologies for Russia, China, the U.S. and Europe

In 2018, global investments in financial technology (FinTech) amounted to $112 billion. Out of this $112 billion, $54 billion came from the U.S., $34 billion from the European Union and $22 billion from the Asia/Pacific region. Global venture capital investments in FinTech amounted to $37 billion, with China in the lead, and the U.S. and U.K. close behind.

Legacy financial institutions are in the best position to reap the benefits of FinTech innovation, due in part to their financial capacity: JPMorgan Chase alone spent $7 billion in tech investments in 2018. These institutions also have enormous market shares, and an ability to create ecosystems that attract and retain customers. Finally, the regulatory structure that exists in the U.S. and worldwide supports the movement of financial transactions through credible legacy institutions. Regulatory barriers to entry are high. Similarly, the global financial system protects countries that dominate it. It is therefore important to consider the relationship between FinTech innovation with regard to both legacy banks and countries.

Facebook's Libra

One key development recently announced is Facebook's new digital currency: the Libra. This cryptocurrency could piggy-back Facebook's network of 1.5 billion daily active users for quick, widespread adoption. Moreover, Facebook already has 27 partners signed up for its Libra project, including Visa and MasterCard, and is looking to expand to 100 partnerships by the end of 2019. If the Libra manages to take-off and scale effectively, it could have major implications for the global financial system. Monetary authorities and politicians alike in the U.S., Europe and Japan recognize the Libra's potential impact on money markets and monetary policy, and appear wary.

China's Response

China has also made tremendous progress in FinTech. One participant noted that this is in part due to the Chinese being generally comfortable sharing personal data in return for more convenient services, financial and otherwise. Chinese people of all socio-economic statuses use WeChat and Alipay payment mechanisms, which has spurred financial inclusion. Chinese banks use Alipay because it provides a trustworthy remote identification system. As for growth opportunities, as firms like Alibaba and Ant Financial look abroad, they will likely turn toward emerging market countries similar to China to expand.

The Perspective of Regulators

Regulators are being influenced by technology as well. Global regulatory authorities are becoming data-driven organizations, tracking digital footprints to become more predictive than reactive. Regulators are also taking advantage of regulatory sandboxes to learn from the technology companies they admit into such programs. Moreover, quasi-regulatory sandboxes like the Global Financial Innovation Network allow cross-border cooperation in financial innovation, underlining the notion that FinTech development and regulation have become increasingly global in nature.

Importantly, how regulators draft rules is likely to change as a result of technology. One key development in this area has been machine-readable rulebooks. Regulators are now working with the private sector to allow machines to read rulebooks and filter them through organizations. One issue, however, is that there are 200 rulebook revisions daily across 2,500 rulebooks globally. Another key issue is that machine learning algorithms often lack explainability. They are not linear models, and therefore there may be no understandable reason as to why a model reaches a particular conclusion. Rules must be developed to address this weakness. Artificial Intelligence cannot be the sole decision-maker and must be complemented by some human input.

Finally, financial regulators will increasingly focus on cyber risk going forward. As financial service systems become increasingly digitized, they also become more reliant on the proper functioning of technology. It is therefore critical to consider how firms handle cyber risk, and to ensure that they have appropriate security in place.

Financial Inclusion

Participants expressed no doubt that digital technology can and will facilitate greater global financial inclusion. Digital technology is not the only important factor in this development, however. Increasing financial inclusion will require greater financial education, as well as partnerships between financial institutions, the public, FinTech firms and consumer goods companies (which have relationships with underbanked consumers), among other actors.

Conclusions

Through open, multilateral discussions, participants exchanged ideas and insights about critical global financial challenges and opportunities facing Russia, China, the U.S. and Europe today, and the profound impact of these challenges on the relationships among these great powers. The discussions made clear that the world is coming to an inflection point. The pace of change in technology, economics and politics has grown much faster in recent years, and the issues the world faces have grown increasingly complex. In this context, the international system needs to revive diplomacy and expand the channels of communication between policymakers and thought leaders alike. Over the past two years, these channels have shrunk drastically. It is just as important for Russia and China to proactively communicate with the U.S. as it is for the U.S. to reinitiate dialogue with Russia and China. Some participants noted that one key factor here is for the U.S. to begin viewing China as a long-term strategic partner rather than an adversary.

Global Cooperation

More must be done to evaluate the consequences of global political and economic fragmentation for major powers, and to avoid fragmentation of the world into multiple blocs (e.g., a continental Eurasian bloc, a maritime Pacific bloc). More global cooperation is needed, and solutions to the world’s problems will require both horizontal communication between countries, and a more attuned approach to vertical communication to better understand the grievances of the poor and middle class. Leadership in the U.S., in particular, should be able to articulate effectively to the public (domestic and abroad) a long-term, strategic vision for the U.S. and its role in the world order. In the absence of this leadership, Russia, China and the European Union should step up and encourage earnest collaboration in the international system. Disruption is neither a leadership position nor a viable long-term strategy.

Existing multilateral organizations, unfortunately, do not appear able to provide this leadership. Bretton Woods institutions should be reformed to reflect the multipolar reality of the world. Russia, China and other countries cite issues with representation, and compromise here could be highly beneficial. Similarly, the European Union, a large multilateral body, should focus on the positives that the Union system has delivered to its citizens over the past decades. Today, negativity seems to drown out more optimistic narratives.

So how to encourage greater global cooperation on key issues? A two-pronged approach may be necessary: 1) limit the current damage, and 2) identify areas where cooperation can be restored. With regard to the first, the idea that interdependence inevitably brings the world toward greater cooperation is not accurate. Leaders need a better understanding of how decoupling is happening between their countries, from universities to business supply chains. They also should try and maintain as many connections as possible and use them to develop cooperation. Moreover, people-to-people relationships at all levels should be maintained, including visas for student exchanges and tourism, and business relations.

With regard to the second, leaders from all sectors of society should use existing connections to identify "islands of cooperation" and turn them into "archipelagos" to stay ahead of emerging problems. Too many politicians and institutions are fundamentally behind the times, stubbornly sticking to old solutions that are no longer suitable in today's world. This is particularly true with regard to new technology, where overly optimistic thinking could be dangerous. Unintended consequences should be termed unanticipated consequences, as "unintended" suggests they were not considered in advance. The world must stay ahead of emerging problems.

China, and U.S.-China Cooperation

Participants noted that China's policymaking should have a more global perspective, and consider how it can enhance global economic cooperation and meet global standards on issues such as corruption and sustainable economic growth. China's investment model has worked well for China but not for its image abroad, and may well receive significant pushback from individual countries and collectively if reforms are not implemented. Initiatives such as the BRI could be a source of cooperation rather than friction between China and the U.S., if China for example shared more information about it with the U.S. Potential cooperation could include the U.S. providing technical assistance and capacity-building for institutions, while China provides infrastructure development.

In the area of financial services and tech innovation, American companies like Amazon and Citibank could work with Alibaba and other Chinese companies to find common ground. Technology protectionism has been a source of tension between the countries in the past. To prevent decoupling, Chinese companies need to work with American companies, and the U.S. needs to enhance its infrastructure development work abroad. This will assuage the current perception that only Huawei can sell to rural areas globally, and that the American private sector is not cost-effective. In the Asia/Pacific region, emerging market countries should not have to choose between partnering with either the U.S. or China.

Russia, and U.S.-Russia Cooperation

Participants noted that Russia has become a lot more focused on security, and this could be a fundamental long-term flaw. The country should focus instead on high-tech investments, and its response to U.S. sanctions should be to make its investment climate as welcoming and transparent as possible. In terms of U.S.-Russia relations, several participants noted that the U.S. should rethink its sanctions regime. Current U.S. hardline policies do not appear to be achieving their intended objectives and may be detrimental to American businesses abroad. Overall, more communication and collaboration are needed between the U.S. and Russia on issues such as arms control, cyber security, the future of the Arctic region and Middle East policy. These are all areas where islands could be turned into archipelagos.

Cooperation on Financial Issues

One area of collective interest, and potentially effective collaboration, for Russia, China, the U.S. and Europe is on global financial sector issues. Financial inclusion (for individuals and countries) and combating terrorist financing are certainly areas of mutual benefit, as is the establishment of basic guidelines for digital identities that can be honored in all jurisdictions.

Some participants warned that the global economy and international financial system should prepare for another bubble to burst in the coming years. Leading powers will need to work collectively and preemptively to enact policies that will protect the most vulnerable populations from this next crisis, including planning how the IMF will act as a backstop to countries in peril. Leading powers should also increase cooperation around FinTech issues, in order to better handle the systemic challenges that will come from innovations such as the Libra.

While participants noted that the relationships that the U.S. has with both Russia and China are fraught, they collectively agreed on the critical importance of thoughtful, constructive dialogue and collaboration in this tense global context. In each of the areas noted above, FSVC as well as symposium participants will be looking for ways to advance these policy recommendations and bring them to the attention of responsible public officials and thought leaders.

Annex I – List of Participants

1. **Anatoly Aksakov** is Chairman of the State Duma's Committee on Financial Markets and President of the Association of Regional Banks of Russia.

2. **Deana Arsenian** is Vice President of International Programs and Program Director for Russia and Eurasia at Carnegie Corporation of New York.

3. **Michael Creed** is Senior Manager of Policy and Strategy at the Dubai Financial Services Authority.

4. **John L. Douglas** is Senior Executive Vice President and Chief Oversight and Advocacy Officer at TIAA, and former General Counsel of the U.S. Federal Deposit Insurance Corporation (FDIC).

5. **Nancy Gallagher** is Director of the Center for International and Security Studies at the University of Maryland.

6. **Evgeny Gavrilenkov** is formerly a Managing Director and Chief Economist at Sberbank CIB.

7. **Harry Harding** is concurrently a University Professor and Professor of Public Policy at the University of Virginia and Yushan Scholar and Adjunct Chair Professor at the College of Social Sciences of National Chengchi University in Taipei.

8. **Maria Ivanova** is President and Chairman of the Management Board for AO Citibank, Russia.

9. **Charles E. Kilbourne** is a Managing Director and Secretary of the Corporation of FSVC.

10. **Anna Kireeva** is a Faculty Member, Asian and African Studies, at the Moscow State Institute of International Relations (MGIMO University).

11. **Ann Lee** is an Adjunct Professor of Economics at New York University.

12. **Wei Li** is a Professor of Economics at the Cheung Kong Graduate School of Business in Beijing.

13. **Syaru Shirley Lin** is a member of the founding faculty of the Master's Program in Global Political Economy at the Chinese University of Hong Kong. She currently serves on the board of Goldman Sachs Asia Bank, and was previously a Partner at Goldman Sachs.

14. **Yaroslav Lissovolik** is Chief Analyst at Sberbank in Moscow.

15. **Angela Mancini** is a Partner at Control Risks in Singapore.

16. **Denis Maslov** is a Business Risk Specialist at UBS in Zurich, Switzerland.

17. **Alex Rodzianko** is President & CEO of the American Chamber of Commerce in Russia.

18. **Klaus Segbers** is Director of the Center for Global Politics at the Free University of Berlin.

19. **J. Andrew Spindler** is President & CEO of FSVC and a Board member of the Dubai Financial Services Authority. He was formerly a Senior Vice President at the Federal Reserve Bank of New York.

20. **Mercina Tillemann** is the Chief Operating Officer of the Global Blockchain Business Council (GBBC).

21. **Ivan Timofeev** is Director of Programs at the Russian International Affairs Council and heads the Euro-Atlantic Security program at the Valdai Discussion Club.

22. **Mikhail Troitskiy** is Dean of the School of Government and International Affairs at MGIMO University.

23. **John L. Walker** is a retired Partner at Simpson Thacher & Bartlett LLP, where he practiced banking law. He is an expert on the policy and regulatory framework for financial systems.

24. **Andy Xie** is a Shanghai-based independent economist focused on financial and economic issues in China and Asia.

25. **Yang Zhou** is Chief of the Corporate Finance Department at the China Securities Regulatory Commission (CSRC).