2009 - 03 - 31 Daily news.

# A new global financial architecture

## Response to global financial crisis

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The global financial system worked out at Bretton Woods immediately prior to the conclusion of the Second World War has undergone many upheavals.

Since the United States replaced Britain as the world's strongest economy and political power it is obvious that it dominated the Bretton Woods Conference. In fact, the United States managed to take key decisions on international finances even ignoring and side-lining Britain and its Finance Minister celebrated economist John Maynard Keynes. As Richard Peet noted in his The Unholy Trinity. The IMF, World Bank and the WTO, "Although Bretton Woods resulted from American and British collaboration, the USA dominated the Conference and directed it according to its national interests. The USA emerged from Bretton Woods as an unchallenged hegemonic world power.'

### Gold standard

The International Monetary Fund was established as the central institution of the international monetary system. The IMF decided to use a gold standard in international transactions and the dollar was pegged to gold at 33 dollars an ounce. Though Sterling pound also remained as a fixed currency by 1947, the dollar became the single reserve currency.

Following the Vietnam War, President Nixon delinked the dollar from gold and the entire Bretton Woods system collapsed. However, the dollar continues to be the reserve currency. Due to the heavy national debt of the United States and the instability of the dollar calls have been made of late to replace the dollar with a basket of currencies. Even now many countries have been using other currencies in their bilateral and multi-lateral transactions. The Euro, which celebrated its 10th anniversary recently, has emerged as a powerful contender for the position of a reserve currency. Calls have also been made by Iran and certain Latin American countries to replace dollar transactions with those using the Euro.

### Dollar as reserve currency

Since the dollar is the reserve currency many nations including China, Japan and India have used their surpluses to buy US Treasury Bills. Since a devaluation of the dollar, which is vulnerable now, would be detrimental to these countries, they are now moving on to diversify their surplus by accumulating Euro funds.

The present economic and financial crisis which originated and spread through the globe has renewed the call for replacing the dollar as the reserve currency.

The People's Bank of China, Governor, Zhou Xiaochan recently called for a radical reform of the international monetary system in which the dollar would be replaced as the main reserve currency. According to him, an international financial system based on a single currency has two main drawbacks. First, the reserve currency status of the dollar helped to create global imbalances because countries with surplus funds bought US Treasury Bills allowing the US to go on a borrowing spree and spending beyond its means delaying the burst of its housing bubble. Second, the country issuing the reserve currency faces a trade off between domestic and international stability which may harm the global economy.

### Special Drawing Rights

A few days ago, the Kremlin issued an official statement called for the creation of a supra reserve currency widening the use of reserve currencies or using the, Special Drawing Rights (SDR) as a super reserve currency.

The SDR is an artificial currency created by the IMF in 1969 to supplement existing reserves of member countries. A few days prior to the Kremlin call Kazakh President Nursultan Nazarbayev proposed a global currency called the "acmetal".

On March 19, 2009, the Commission of Experts of the President of the United Nations General Assembly chaired by Nobel laureate Joseph Stiglitz recommended the creation of a new Global Reserve System, which may be viewed as a greatly expanded SDR. It commented thus; "The dangers of a single-country reserve system have long been recognized, as the accumulation of debt undermines confidence and stability.

But a two (or three) country reserve system, to which the world seems to be moving, may be equally unstable. The new Global Reserve System is feasible, non-inflationary, and could be easily implemented, including in ways which mitigate the difficulties caused by asymmetric adjustment between surplus and deficit countries."

### Global recovery

The interim report of the Stiglitz Commission has listed 10 immediate measures essential for global recovery. They include strong, coordinated and effective action by developed countries to stimulate their economies, additional funding for developing countries, creation of a new Credit Scheme, allowing more policy space for developing countries, rectification of incoherencies in policies governing trade and finance, avoiding protectionism as a policy response to crisis, opening developed country markets to exports from least developed countries and improved coordination of global economic policies.

In order to implement deeper systematic reforms in the international financial architecture, the Commission recommends major reforms in the International Financial Institutions to give more voice to developing countries and ensure greater transparency, the establishment of a Global economic Council at a level equivalent with the General Assembly and the Security Council, better and more balanced surveillance, changes in financial market policies including the need for regulation of derivative trading, regulation of credit rating agencies and more stable and sustainable development finance.