Financial and monetary crises

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Summary : Financial liberalization has meant that governments have lost their ability to control the global flow of capital, thereby surrendering monetary and economic policy sovereignty to investment firms, sovereign funds and large banks. International Monetary and financial system is still in crisis, with a lot of world disequilibrium, the difficulty to furnish international liquidities and the existence of sovereign funds. There are a lot of proposals in order to fight the financial and monetary crises.

Dollar, debts, financial liberalization, IMF, Euro, financial strategies

Financial and Monetary crises are the main recurrent problem of capitalism system. The financial systems are based on financial plan on future, but when promises are not kept the markets experience a very strong risk aversion. Sometimes, this crisis is qualified of systemic and it is the case today, more important than the 1929 crisis. The 1970s crisis was the inflation consequence with the oil shocks. Then, the shareholders received more money and the wages were proportionally reduced. Today the situation is different. The enterprises are obsessed by their profit rate and then they reduced their equity capital and support more debts. At the same time, the financial innovation tried to transfer the risks. There is now, as a result, a system of generalized debts. Then, the crisis is a long-term crisis. How will the volume and direction of financial flows change in the new environment? Will a new balance of power emerge between creditor and debtor countries? There is an apocryphal story that Zhou En-Lai, when asked by Kissinger about the impact of the French

Revolution, commented 'it is too early to tell'.

Financial liberalization has meant that governments have lost their ability to control the global flow of capital, thereby surrendering monetary and economic policy sovereignty to investment firms, sovereign funds and large banks. Whether banks are engaging in 'moral hazard' or holding governments to ransom is a question that economic liberalism cannot seriously explore because of the primacy it gives to rational (consumer) choice in markets. An enormous discrepancy exists between an increasingly sophisticated international financial world and the lack of proper institutional frameworks to regulate it at the national and multilateral levels. The inevitability of future crises makes the re-regulation of capital a global imperative. The most powerful nation-state--the USA--is in hock to creditors which mainly comprise Sovereign Wealth Funds and central banks of many, increasingly emerging 'large' economies. Into the euros zone, it exists at the same time creditors and debtors members. Then, it is difficult to predicate the movements of financial flow.

This is unprecedented though some creditors, like China and Japan seem to remain national economies. The clear challenge facing the G20 Meeting is to bring awareness to the United States that the system is in danger and that the US is no longer dictating policy[1]. For the last decade, China, the creditor nation in the world must sit in the hall while debtor bankers make decisions, issue orders, change structural procedures, and pretend to be in charge. However, never in financial history have debtors remained in power, and this is no exception. Contemporary business bankruptcies are arenas for creditors and debtors to handle their negotiations in a systematic manner under national laws in national courts. Yet when a sovereign state defaults on its debts, there is no

[1] There are 20 members of the G20 organization. These include the finance ministers and central bank governors of the following countries: Argentina, Australia, Brazil, Canada, China, France, Germany, India, Indonesia, Italy, Japan, Mexico, Russia, Saudi Arabia, South Africa, South Korea, Turkey, United Kingdom, United States. The 20th member is the European Union, which is represented by the rotating presidency and its European Central Bank. In addition to these 20 members, the following forums and institutions participate in G20 Meetings: International Monetary Fund, World Bank, Intl Monetary & Financial Committee, Development Committee of the IMF & World Bank.

equivalent forum to adjudicate the disputes between creditors and the state. During the 2008 presidential campaign, Barack Obama stated, “It’s pretty hard to have a tough negotiation when the Chinese are our bankers. Chinese officials and think tank analysts have suggested that Beijing use its dollar holdings to prevent American protection- ism, acquire strategic assets, and ward off international pressure on the Tibet issue.

HOWEVER, THESE EMERGING NATIONS, THESE CREDITOR NATIONS, THESE SMALLER LESS POWERFUL NATIONS, WHICH COINCIDENTALLY DO NOT HAVE MILITARY FORCES OF THEIR OWN, HAVE NO GLOBAL BANKING POWER, HAVE NEVER HAD ANY GLOBAL BANKING POWER, BUT NOW ARE DEMANDING GLOBAL BANKING POWER. However, much bigger tasks come. The United States must accept that the US Dollar can no longer function as before, cannot serve as the primary and only global reserve currency, and must share reserve currency status with other regionally crucial currencies. As the United States continues to run large deficits, many other commentators believe that its power is another bubble that will soon pop. Creditor nations demand a more solid reliable global reserve currency, or currencies. They increase their power, but they it is still difficult for them to exchange their dollars against other money or products. Their freedom is reduced. American diplomats wanted to lock foreign countries into further dependency on paper dollars. The rest of the world sought a way to avoid giving up real output and ownership of their resources and enterprises for yet more hot-potato dollars. The United States still possesses alternative sources of credit—both foreign and domestic. The yields on U.S. government debt, after falling to historic lows in early 2009, remain well below the historical mean—because the United States is still perceived as a safe haven compared with the alternatives. If China scaled back its purchase of U.S. assets, the dollar would inevitably depreciate against the renminbi. Any dollar depreciation triggers capital losses in China’s external investment portfolio. The issue of sovereign wealth funds represents an excellent test for the ability of debtors to resist creditor preferences. Consistent with the traditional preferences of capital exporters, Chinese officials wanted U.S. officials to protect the value of China's dollar- denominated assets

We have tended to treat states as either creditors or debtors, instead of being co-responsible partners. That has to change. The most obvious IMF reform would be to readjust the voting rights of member states to reflect the changes in the global balance of economic power. This should not only include greater influence for - and capital contributions from - emerging giants such as China and India, but also, in keeping with Manuel's prescription, an increased role in decision making by the less developed countries. The least irrelevant news was not good at all: The attendees agreed to quadruple IMF funding to $1 trillion. However, anything that bolsters IMF authority cannot be good for countries forced to submit to its austerity plans. This is quite a contrast with the United States, which is responding to the downturn with a giant Keynesian deficit spending program, despite its glaringly $4 trillion debt to foreign central banks. The United States and Britain would never follow such conditionality. Mr. Obama's stimulus program is Keynesian, not an austerity plan, despite the fact that the United States is the world's largest debtor.

Today, International Monetary and financial system is still in crisis, with a lot of world disequilibrium, the difficulty to furnish international liquidities and the existence of sovereign funds (2000 billions for China, 200 for Brazil, 100 for Algeria). It is fragile and unable to fulfil its central function, a stable environment. With the external shocks, it is necessary to reduce the capital volatility. The financial operators need confidence, but structural weaknesses and uncertainty on the liquid assets subsists. Debtor countries must borrow a trillion from the IMF not to revive their own faltering economies, not to pursue counter-cyclical policies to restore market demand (that is only for creditor nations), but to pass on the IMF "aid" to the poisonous banks that have made the irresponsible toxic loans.

With the monetary zone, it is essential to reduce moral hazard. It is the main problem of the Euro Zone. It is then essential to improve the predictability, the credibility and the stability of the system. In the meeting we had with Dominique Strauss-Kahn last Wednesday in Paris, he explained that dollar is resilient, SDR are not still able to be an international money, Euro has to solve its problems. International money can be built on the basis of a basket of moneys only when it will be proven to be more resilient than the dollar system. The evolution of dollar is more important than the evolution of US economy.

The international financial crisis is not finished. However, it was the most important crisis, more important than 1929. But the cooperation of the world governments and G20 has produced some solution that are, in the short run, sufficient to reduce the effects, mainly thanks to the international solidarity. Today, the interdependences are so important, that a reduction of a country growth provokes a recession effect on other parts of the world[2]. A considerable effort from the international community was made against the crisis, by the governments: more than 1000 billion dollars. The most interesting lesson is the government's capacity to be engaged in a cooperation process. In 2009, all the States and Regional Unions decided to prefer solidarity compared to individual strategies. All of them, decided to follow the IMF recommendations. In today's world, the easiest way to obtain wealth by old-fashioned "primitive accumulation" is by financial manipulation. This is the essence of the Washington Consensus that the G-20 supports, using the IMF in its usual role as enforcer. That is why the United States has not permitted an IMF advisory team to write up its prescription for U.S. "stability." The Washington Consensus is only for export. ("Do as we say, not as we do.")

The public debt in USA is still important, the household and enterprises debt are very important, more than 50.000 billion dollars. It was the same at the end of the last world war, with a 250% of GDP debt. But USA decided to take time and to reduce the debt in 15 years. It is not essential to reduce the debt too quickly, because of the recession's effects on the world economies. If you reduce all expenditures, the domestic demand is reduced and the growth must be based only on foreign demand. But to obtain this possibility, the emergent economies

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[2] Fontanel, J., Henriques, A. (2007, 2010), A Globalizaçao em Análise: Geoeconomia e Estratégia dos Actores Instituto Piageto, Lisboa. 2007, 2nd. Ed. 2010

must have a strong growth and must choose the European exports. It is not evident. The euro zone is considered today as a dangerous zone. Then, if there is a political will for a common industrial policy, in the same way than China and USA, it will be easier to obtain the financial markets' confidence.

The only duty of European Central Bank is to work on inflation control, but in this particular situation it has decided to reduce drastically the interest rates. However today, prices are determined at Beijing, New Delhi, Moscow or New York. Then, this solution is not clearly a good policy. Moreover, the problem of the crisis in Greece, Spain, Portugal or Ireland creates a new situation. Now bankrupt without financial backing threatens some States. Mediterranean Europe countries are mainly concerned. They had some advantages with euros, to obtain interest rates from 10 % to 3 % inside the Euro zone. But at the same time, there is important divergence of productivity inside the zone, with various wages policies and an absence of budget solidarities.

Today, Germany doesn't want to follow this way, but it needs to maintain euro zone that is threatened by an explosion. In this case, the crisis conduces to a lost of competitiveness, a reduction of wages and salaries, and Europe enters in a new and intense economic depression. European Union needs to establish some European bonds or assets in order to pay its debts. It is impossible for German economy to obtain some good economic results inside a Europe with a deep depression. The interdependences between euro members are necessary. It is useful to create a European Fund able to issue some financial securities bought by institutional investors and create a fiscal system on the basis of carbon tax. Finally, it will be essential to reduce the income inequalities and to produce a social protection controlled directly by the Parliaments.

Now, all countries have to act in order to reduce the importance of the crisis. There are a lot of proposals to solve this financial crisis[3]. Michel Aglietta[4] proposes to finance investment in technologies for

[3] Fontanel, J. Les maîtres-penseurs de la crise financière mondiale, Annuaire Français des Relations Internationales, AFRI, Paris, 2010.

[4] Aglietta, M. (2007), Désordres dans le capitalisme mondial, Odile Jacob, Paris. Aglietta, M., Rigot, S. (2009), Crise et rénovation de la finance, Odile Jacob, Paris.

climate changes and on the cost of health. THEN, IT WILL BE ESSENTIAL TO USE FISCAL INSTRUMENT, for Europe, a European fiscal instrument. Developing new technologies implies taking a lot of risks and the taxes will be useful in order to finance research and development. A coordination of fiscal systems in Europe and the will to propose some industrial policies is necessary. If it is important to think about the reduction of deficit, still, it is important to conceive economic growth for the well being and welfare of the citizens. European Union has to be engaged in common solidarities, with a common budget policy and resources transfer for new investments. For IMF[5], we need large economic entities to solve new problems: there is no individual economic solution. When China obtains a strong economic growth, problems on raw materials and energy supply arise. China has changed its own rules, with a control of foreign investments, a research policy and the will to improve the domestic demand.

In this situation, Europe has certainly a way to work with Russia. The Russian economy is very interesting for its production of energy, the raw materials, the quality of its researchers, and its high technology. Because the financial markets have a strong risk aversion, some economic agreement between Russia and Europe should be signed for confidence between partners and for international community. For instance, a large agreement on contracts on energy (petrol, gas, nuclear, solar) would be very interesting for the two parties. In this case, Europe would reduce its risks of economic difficulties in the oil supply and at the same time Russia would obtain some advantages in technologies transfer or in the equipment furniture. It would be very interesting to create a link between rubble and euro in this kind of economic exchange, in order to reduce speculation risks[6] and to be more independent from the dollar speculation.

More important, it would be very interesting to implement joint productions and research in order to organize a new flow of new products, for a new XXI century.

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[5] IMF (2009), Fighting the global crisis. Annual Report 2009, Washington.

[6] Coulomb, F., Fontanel, J. (2006), Spéculation et instabilité financière internationale ,in « Des flux et des territoires. Vers un monde sans Etats ? Sous la direction de Bernard Jouve et Yann Roche, Presses de l'Université du Québec, Montréal.

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