

International Financial Crisis & Single World Currency

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India's Last 5 years

- GDP growth ~9%
- Forex reserves \$300B+
- Sensex Jan 2003-Dec 2007 ⇒ 500%↑

India 2008 ?

- Inflation rose to double-digits
- Growth slowing
- Sensex down 50%
- Foreign Institutional Investment
 - 2007 up \$19B
 - 2008 down \$9B
- Rupee
 - Down 10% against USD
 - Down 17% against the Euro

Critical External Factors

- Spiraling oil prices – 3x in 5 years
- Rising food prices -- 2x since 2005
- International Financial Crisis

Subprime Crisis

- World's financial markets in tailspin
- Direct losses by global banks \$500B+
- Stock market losses \$11 T in Jan-Jun '08
- Real estate values down \$3.7 T in 2 years
- USD lost 25% vs. Euro
- Financial institutions threatened
- Global GDP growth to slow 50% in 2008

Accusations abound against

- International bankers
- Commodity speculators
- Multinational oil & food corporations
- Petroleum exporters, hedge funds
- Debt-ridden American public
- Energy-hungry China
- None are sufficient to explain what is happening

Root Cause: Globalization

- Revolutionary changes transforming global society, the global economy & global financial markets
- Its speed & magnitude have reached critical stage after 1970
- Energies exceed capacity of national level institutions

Globalization of Financial Markets

- World trade ↑ 4x since 1990
- FDI ↑ 7x since 1990
- Int'l bank loans ↑ 150x 1975-08 = \$40 T
- Int'l fin assets ↑ 14x 1980-2006 = \$167 T
- Foreign ownership of equities = 25%
- Foreign ownership of US T-bills = 60%
- Forex Reserves ↑ 10x from 1990 = \$7.5 T

Nation-State System

- Source of energy & instability in 20th C.
- Inadequacy of global governance based on sovereign nation states
- Balance of power ⇒ WWI & WWII
- UN System
- Cold War & Arms Race
- Competitive security system
- International financial instability

Beyond the Nation-State

- Unification of Europe
- Unified European Army
- Calls for global military force & cooperative security system
- Evolution of Int'l Financial System

Panic of 1907

- Rapid industrial & commercial expansion
- Flooded capital markets with huge surplus of money seeking lucrative returns
- Absence of effective regulation
- Highly leveraged funds from banks
- Spiraling equity prices lured even small investors seeking windfall profits

US Federal Reserve System

- Established in 1913 to regulate the banking industry & prevent speculative squandering of the nation's savings
- Decentralized structure
- Supervisory Board in Washington
- 12 Regional Banks chaired by bankers
- Regions had almost complete independence from Washington

Great Crash & Great Depression

- Problems of 1907 returned in 1929
- SEC established in 1934
- Fed restructured in 1935
 - Concentrating power in Washington-based, government-appointed board of governors
 - Modified structure was highly effective
 - Stable basis for domestic economic growth

Bretton Woods & Its Aftermath

- Nation-centric system
- National central banks + IMF
- Parallel to original US Fed
- Decentralized authority
- Chief function was coordination
- Fixed exchange rate system
- Stable basis for int'l financial for 25 yrs

End of Bretton Woods ~ 1970

- Rapid growth of international financial activities exposed inadequacies
- Exchange rate management inadequate to meet the needs of a rapidly expanding global economy
- Gold Standard abandoned by USA
- Fixed rate exchange system abandoned
- Each country left to fend for itself

Rapid Deregulation & Globalization

1970s: Financial deregulation of banks & offshore banking

1980s: Globalization of the bond markets

1990s: Globalization of banking & equity markets

1995: Globalization of trade under WTO

Globalization of risks

Rising Financial Instability

1979: Latin America's southern cone

1982: Developing country debt crisis

1985: US Savings & Loan debacle

1989: Japanese asset bubble burst

1992: Europe's ERM crisis

1994: Mexican crisis

1997: East Asian crisis

1998: Russian crisis

1999: Brazilian crisis

High Cost System

- Periodic catastrophic losses
- Global financial transactions ~\$400 b/yr
- Higher domestic interest rates
- Interest differential on forex \$100+ b/yr
- High forex reserves for protection
 - Developing countries > \$4.5 trillion
- Lost investment opportunity cost
 - India 3.5-4% of GDP not invested
- Negative or low rates of GDP growth
 - 24 emerging markets GDP ↓ 5-8% in GDP following crises
- Reduce value of assets due to currency risks
 - Absence of long term mortgages in Latin America
 - Euro raised asset values by \$5-11 trillion 1993-2003
 - SWC raise asset values ~\$36 trillion

Life Repeats: 1907, 1929, 2008

- Highly leveraged, speculative market
- High volatility
- Highly liquid capital
- Ever-expanding complexity of markets
- Rapid innovation of new financial products
- High susceptibility to contagion
- High systemic as well as individual risk

“Financial liberalization and innovation have rendered national boundaries irrelevant. If regulation was necessary within national boundaries, then it is now equally necessary in the international market.”

*Economic Report to US President Clinton
September 1998*

Partial Measures

1969: IMF SDRs as international reserve asset

1974: Basel Committee to coordinate policies for banking regulation.

1987: International Organization of Securities Commissions to set minimum standards for securities firms.

1987: Tripartite Committee of banking, securities & insurance regulators.

1999: Financial Stability Forum to establish consistent international rules

**National level financial management is inadequate
More radical steps are needed**

Idea of a World Currency

- **Bretton Woods 1944:** Britain & the USA proposals for world currency
- IMF created a fixed pool of national currencies to maintain price stability, **not** a world central bank capable of creating money.

Richard Cooper (1985)

- “National level monetary system insufficient in an age of globalization of communication, transport, technology, trade, corporate strategy, banking and investment.”
- Common currency for all the industrial democracies
- Common monetary policy
- Joint Bank of Issue

Robert Mundell (2002)

- Proposed a global central bank to issue a global currency backed by reserves of dollars, yen, euros, and gold.

“The benefits from a world currency would be enormous. Prices all over the world would be denominated in the same unit and would be kept equal in different parts of the world to the extent that the law of one price was allowed to work itself out. Apart from tariffs and controls, trade between countries would be as easy as it is between states of the United States. It would lead to an enormous increase in the gains from trade and real incomes of all countries including the United States.”

Joseph Stiglitz (2006)

- Nation-centric financial system is partial and flawed, because it concentrates power at the national level and leaves even the strongest currencies subject to external impacts beyond the control or power of national central banks to regulate. It supports a competitive system of global trade that necessitates the generation of deficits in some countries to offset the surpluses in others. Stiglitz

“Adoption of SDRs as a reserve currency by the national central banks could pave the way for the eventual creation of a **single world currency.**”

Paul Volcker

“If we are to have a truly globalized economy, with free movement of goods, services and capital, a world currency makes sense. That would be a world in which the objectives of growth, economic efficiency, and stability can best be reconciled.”

Global Social Evolution

- Defect of partial systems—political, military, economic or financial
- Only a comprehensive and inclusive system that embraces the whole can be immune from threats and instability.
- Trade & Finance are only parts of society
- To achieve the goals of maximum stability & maximum growth, a global financial system must be fashioned as an integral part of a greater whole which is global governance.

Money is Social Energy

- Social energy grows by movement.
- The more rapidly it moves, the faster it grows.
- Organization transforms energy into power
- Insufficient organization \Rightarrow short circuit or explosion

Money

- Influences every field of human existence, not merely production and living standards.
- Integrated with politics, security, education, environment, science, health, etc.
- A truly global financial system can advance the entire agenda of human progress
- Instrument for harnessing the unlimited potentials of society

The First Step

A single world currency is not the last step in global financial management. It is the first logical step in the evolution of a truly democratic system of global governance, peace and security for all nations, and universal prosperity.