Reform des internationalen Währungssystems (R. Guttmann)

1) Wie bewerten Sie die aktuellen Vorschläge zur Reform des Internationalen Währungssystems, insbesonders zur Rolle des IWF?

Since the breakdown of the Bretton Woods system in the early 1970s there have been several regulatory adjustments of the international monetary system (IMS):

•The Kingston Accord of 1976 allowed countries to adopt the exchange-rate regime most to their liking, leading to a myriad of alternatives centered around “managed floating” (i.e. flexible exchange rates subject to some form of government regulation). Since then the leading capitalist powers have grouped together - first as the G-5, then as the G-7, now as the G-8 (including Russia) to move jointly towards better international policy coordination. But efforts in this direction have stalled. The target-zone experiment for the key exchange rates of dollar, mark, and yen has atrophied since its inception in the Louvre Agreement of 1987, as each of the major powers has found it politically unpalatable at home to carry out the kind of monetary and fiscal policy adjustments or institutional reforms required in the interest of international coordination. As a result we have faced continued, even increased volatility in the key exchange rates which have forced the G-7 countries repeatedly to abandon their target zones.

•While capital controls have been phased out across the globe to spur on international capital movements, central bankers in the key nations have gradually extended regulation of the Euromarket, the nerve center of international capital movements and as such the key engine behind the globalization. This began in 1975 when central banks, under the auspices of the Bank for International Settlements (BIS), approved a division of labor among themselves with regard to supervision of

transnational banks operating in the Euromarket and with regard to crisis management in the Euromarket - the socalled Basle Concordat. In the Basle Accord of 1988 the central banks went a step further and imposed a uniform minimum capital-asset ratio of 8 percent on transnational banks, including their Euromarket operations. That socalled "Cooke ratio" was adjusted for risk, in effect requiring more capital for greater risk in the asset portfolio of the bank. Different bank asset categories were given different weights, depending on risk. Since this risk categorization of assets proved to be in many instances flawed, misleading, and counterproductive (e.g. underestimating risk of certain assets and thereby encouraging banks to take on too many of those), the BIS urged last year to reclassify these risk categories more effectively and more realistically.

•The debt crisis of the less developed countries during the 1980s transformed the International Monetary Fund (IMF) into a lender of last resort for developing economies on the brink of default. This role has enabled the IMF to expand its resources, its scope of intervention, and its range of lending programs since then. But the Asian crisis of 1997, which spread subsequently to Russia (August 1998) and Latin America (January 1999), put the IMF on the spot and opened up a push for reform of the IMF. The controversial and at times even counterproductive management of that crisis by the IMF has provoked a groundswell of criticism against the Fund. Critics on the Left have complained that the heavy-handed intervention by the IMFs, especially in the case of Thailand and Indonesia, deepened the crisis by demanding structural reforms and austerity measures which, besides ignoring the cultural and political specificities of those countries, helped make the subsequent downturn worse there. These critics also consider it unjust that IMF actions protect rich investors while at the same time impoverishing millions of already struggling families in Asia and Latin America. Conservative critics of the IMF, on the other hand, worry that the bail-out guarantees extended by the IMF to countries in trouble provide an incentive to irresponsible governments and profit-seeking investors to take excessive risks, the socalled problem of moral hazard.

The reform proposals, which have come out of these post-crisis criticisms, aim to bridge both types of complaints. The idea of having private investors share a bit more in the bailout costs, either by taking some loss or contributing to the assistance of countries in financial difficulties, is not only politically popular. It also makes sense from the point of view of reducing the moral-hazard problem, since investors will be more careful if they know that their mistakes may actually end up costing them. It is also a sensible idea to provide the IMF with "soft" lending facilities (i.e. loans tied to less restrictive conditions) for countries with a good record of structural reforms (e.g. Mexico) and/or countries hit particularly hard by world-market circumstances beyond their own control (e.g. collapsing commodity prices). Such facilities may soften the blows of austerity and structural reforms, typically demanded by the IMF from countries in crisis, by helping to set up social safety nets there. Finally, I like the emphasis which certain reform proposals have put on prevention and early-warning indicators, because crises may be lessened in intensity as a result. This presumes that the countries in questions have the will and the ability to provide better information about their macroeconomic performance to the outside world.

In the end the proposed IMF reforms are quite modest and pragmatic, aimed at better crisis management. They do not fundamentally alter the workings of the current IMS. Yet even those modest reforms have caused much controversy (particularly from a reticent U.S. Congress unwilling to put more money into the IMF unless that institution is scaled back into a short-term lender to countries in need of balance-of-payment adjustments). While I see these reforms by and large as useful improvements, they are far from adequate to cope with the flaws of our IMS as presently constituted. Much more far-reaching reforms are needed to deal with the challenges of unregulated capital flows and variable exchange rates.

2) Welches sind Ihre eigenen Vorschläge zur Regform des internationalen Währungssystems (aufbauend auf Ihrem Buch von 1994)?

Economists usually discuss the international monetary system (IMS) in terms of the appropriate exchange-rate regime and/or possible macroeconomic adjustment processes to external imbalances. This rather narrow view of the IMS ignores two vitally important points about money. One is the contradictory dual nature of money (as both public good and private commodity) which finds a particularly virulent expression in the context of our contemporary IMS. The other is the serious structural flaw of any IMS which is built on national currencies functioning as world money in cross-border transactions, a situation that prevails today.

Money, when analyzed as a social institution, reveals itself as both public good and private commodity at the same time. It is a public good inasmuch as its proper functioning - in terms of smooth circulation, well-balanced creation, and stable valuation - yields such large social benefits that you would want noone to be excluded from those. It is a private commodity inasmuch as it is created by private agents, at this point mostly banks, trying to gain income from that activity. Banks create new money in acts of lending, thus by transforming their zero-interest (or low-interest) excess reserves into income-yielding loans or securities. These two dimensions of money are often in contradiction with each other. For instance, excessive credit supplies by profit-seeking banks can undermine the stable value of money through an inflationary surge or may disrupt the smooth circulation of money by triggering financial instability. This contradiction needs to be managed. Ever since the collapse of the gold standard in the early 1930s this contradiction has come to be managed by the state, specifically its central bank, using a combination of monetary-policy tools, financial regulations, lender-of-last-resort mechanisms, and international monetary agreements for that purpose.

Any central bank, such as the Fed or the ECB, has to use these four dimensions of state management of money so as to maintain its quality as a public good without impairing its private-commodity nature too much. If the private-commodity elements of money become dominant to the point of crowding out money's existence as a public good, our economic system suffers from all the negative consequences of money's commodification into a vehicle for bank profit - more pronounced cyclical fluctuations punctuated by financial crises, greater price instability, and widening income-distribution gaps between rich and poor as the result of increasingly unequal access to money and credit.

We are precisely in such a period now. The deregulation of money has moved beyond its prices (first exchange rates in 1973, then interest rates in 1979/80) to the form of money, spurring the introduction of a whole new generation of private bank money (e.g. money-market deposit accounts, NOW accounts, consumer certificates of deposit, money-market funds). Such privatization of money, usually propelled forward by regulation-evading innovation among financial institutions, has been even more dramatic on the international level. I am thinking here in particular about the Eurocurrency market, a globally integrated private banking network operating with its own payments systems (i.e. SWIFT) beyond the reach of any national central bank. Since its inception in the early 1960s the Euromarket has been the principal conduit for evasion of government taxes and regulations, the locus of speculative attacks on currencies (as a means to change government policy to the benefit of financial investors), and the engine for recurrent global debt and currency crises. Another manifestation of money's private-commodity nature coming to the fore on the international level is the explosive growth of the foreign exchange market (with its own private payments system known as CHIPS) where corporations and financial institutions engage more and more in short-term currency trades for hedging or speculative purposes as if they were placing bets on whole countries.

The combination of Euromarket and currency trading has led to the huge volume of short-term capital movements across the globe in constant search for better returns. This socalled “hot money” has become the central force of the world economy, subjecting national governments to conservative monetary and fiscal policies (lest capital flows out of their countries and currencies) while triggering frequent explosions of financial instability engulfing a region or even the entire globe (e.g. LDC debt crisis of the 1980s). Such a highly privatized and deregulated IMS tends to undermine the world economy, especially since there is no effective monetary authority operating on the global level to assure the public-good quality of money in the international context. The IMF, perhaps the only institution currently existing with the potential to carry out that task, does not operate like a global central bank due to its inability to issue its own currency at will (e.g. Special Drawing Rights) and) and its narrow mandat focusing on lender-of-last-resort assistance to countries in danger of defaulting on their foreign debt.

The second structural flaw of the IMS, as currently constituted, is its reliance on national currencies as world money. National currencies cannot properly function as world money. Economists have a hard time grasping that point, since they focus on the three functions of money which key currencies can carry out reasonably in cross-border transactions between countries. The US-dollar does after all get used as international medium of exchange, store of value (“reserve asset”) and unit of account for globally traded commodities (e.g. oil). But even within that traditional framework it seems clear that the unit-of-account function can only be satisfied by national currencies in a very limited sense, namely as the basis for denominating international prices. When we take the unit-of-account function of money a bit further, namely as measure of value, it is obvious that national currencies, even as dominant a key currency as the US-dollar since 1945, do not represent universal value based on average world-market conditions of production. In other words, our dollar-based IMS lacks an objective value anchor (such as gold used to represent) - the socalled “numeraire” problem. Instead currencies are all valued in terms of each other, a system consisting entirely of relative prices reflecting an ever-changing hierarchy of average national productivity levels and power relations

between countries. If all currencies are valued relative to the dollar, what determines the fair-market value of the dollar? It cannot be simply valued in terms of other currencies, unless you are willing to accept an entirely tautological argument. The neoclassical economic orthodoxy has tried to deal with this problem by invoking the concept of purchasing power parity as the objective fair-market value of currencies. But, in the absence of fully globalized commodities, this concept is difficult to measure accurately. And it applies as an objective value basis only to trade, often deviating from (uncovered) interest parity which is the parallel objective-value measure pertaining to international capital flows. So each currency has two alternative equilibrium prices, an unsatisfactory solution.

It is, however, with regard to the fourth (and usually ignored) function of money, namely as means of payment, that the limitations of national currencies in cross-border transactions fully come to the fore. The means-of-payment function refers to money's ability to settle payment obligations, in particular debts, among countries. The problem here is that in an IMS based on national currencies the country issuing the key currency never really settles its debts with the rest of the world. This point deserves deeper reflection than it is usually accorded. While international transactions occur between individual actors engaging in exchange across borders, from the monetary point of view any such cross-border transaction is one between one country and another country. It is countries in their entirety who pay each other (with transfers of income and thus purchasing power), with ultimate settlement of net debit balances between their respective central banks. But just as no individual market actor can settle payment obligations properly in his own money, so can no country properly pay for its international purchases in its own money. Allowing the US currency to function as world money means in effect that the Americans can pay for their foreign purchases of goods, services, and assets in their own money (which after all is nothing but a paper token, nothing more than a promise to pay). This advantage, a sort of global seigniorage, becomes immediately obvious when we consider that the supply of international liquidity requires the United States to run chronic balance-of-payments

deficits (i.e. net outflow of dollars) which are automatically financed by foreigners willing to hold the dollar as reserve. In other words, the US does not face the same kind of external constraint as everyone else. Apart from the advantage thereby accruing to the United States, such an IMS is inherently asymmetrical. It exempts the US from adjustments to external imbalances and puts that much more burden on other deficit countries. Moreover, since those dollar outflows from the US do not constitute proper settlement of American payments obligations, dollars in international circulation never get destroyed (which happens in domestic circulation when debts are repaid) - the key reason behind the creation and rapid expansion of the Euromarket over the last four decades.

Any IMS based on national currencies is thus flawed. It does not help having the US dollar being challenged by the euro or other major currencies (yen?) for world-money status. Then you have simply two or three key currencies competing with each other and giving its issuers significant seigniorage benefits. In that case you may have even more instability than in single-currency IMS because of large portfolio adjustments destabilizing exchange rates and because of the centrifugal tendency by the leaders to build regional blocs around those key currencies (dollar -> NAFTA area plus Latin America plus parts of East Asia, euro -> Europe and Africa; yen -> Asia) as their zones of influence and means of dominance. This scenario, that of a triad centered on three competing power blocs, is certainly the one we are moving towards, especially once the $450+ billion US trade deficit will start bringing the dollar down.

The confluence of money's private-commodity aspects having come to dominate our IMS and its reliance on national currencies as incomplete world money calls for much more basic reform in the (hopefully not-so-distant) future. Both structural flaws of the current IMS can be resolved by one decisive move, namely instituting a single global currency for all international transactions. In that context it would be useful to go back to Keynes' Bancor Plan of the early 1940s and develop an updated version of it, as I have tried to do in my 1994 book. Such a single-currency plan need not be as radical as the

euro, a supranational money form actually replacing national currencies. It would be easier, in terms of requiring less convergence, if national currencies continued to exist within their respective domestic space. At the same time all cross-border transactions between countries would be conducted in the global currency, with this money being issued and managed by an international central bank (ICB) akin to Keynes' proposed International Clearing Union (thus radically different from the single-purpose IMF).

In my 1994 book *How Credit-Money Shapes the Economy* I explain in considerable detail (especially chapter 15) how such a global-currency system and international central bank could work. There is the issue how this money would be issued as credit-money which requires it to be simultaneous asset and liability and which also calls for its eventual destruction once the monetary circuit giving rise to its creation has been fully completed. There is the question of the supranational payments system, with the international central bank at its center and tying all the nations' central banks together. There is the question of exchange-rate determination, basically a system of fixed exchange rates which would be adjusted by the ICB on the basis of consensual rules shared by all. Those rules would specify performance standards for each member country, permissible levels of external imbalances, and adjustment options for different degrees of imbalance (including changes in the exchange rates). The key here is to have symmetric adjustments between surplus and deficit countries. In my plan a portion of the surpluses recycled via the ICM would be turned into long-term investment funds for countries with more or less chronic balance-of-payments deficits. This would facilitate the catching-up process of lesser developed countries which makes for a more balanced growth pattern of the world economy. The gold standard of the late 19th and early 20th century, the Bretton Woods system during its first two decades, and the European Union's implementation of a single-currency plan all have shown that any system facilitating such catching-up processes provides for overall faster and better balanced growth.

Such a reformed IMS based on a single global credit-money has the advantages of proper state-management of money (to assure its public-good quality and constrain the worst excesses of its private-commodity nature), stable exchange rates, symmetric adjustments, effective debt settlement, and non-discriminatory finance. None of these conditions are assured by the current IMS. The key to my plan is the creation of a new payments system, managed by the ICB at its center and linking all the world's central banks together, which would make the Euromarket and the foreign exchange market obsolete. All this may sound hopelessly unrealistic, but is perhaps less utopian than it may seem at first sight. We are after all in the midst of a technological revolution which may well facilitate the eventual introduction of my plan. As the Internet becomes the central locus of (e-)commerce, more and more of our money will take the form of cybercash, that is electronic money created and circulating on the Internet. This superfast, borderless, and essentially private money form will only exacerbate the problems of "hot money," volatile exchange rates, and crisis-induced adustment processes which fall too one-sidedly and brutally on the debtor countries. In other words, all the problems of our current IMS are likely to intensify with the emergence and proliferation of cybercash. But the new money form will at the same time also point to the solution to these problems in the direction I have suggested above. Since the Internet is a multi-layered structure of software application protocols, all it takes is to add one more layer of encryption software for all cross-border money transfers under the control of a newly created ICB coupled with changes in the Internet address system for easy identification of cross-border transactions.

I am currently writing a book on cybercash where, among other things, I am trying to concretize in some detail how such a ICB-managed payment system for global cybercash might work. It is technically feasible, but requires unprecedented political will and consensus to put into place. That will not come about unless large majorities become convinced of the dangers of our current system and understand its structural flaws. Such conditions may never arise, except in the aftermath of a major structural crisis. Even as serious a financial crisis as the one sweeping through Asia, Russia, and

Latin America a couple of years ago will not suffice in that regard. While that crisis was unique in terms of its speed, scale, contagion capacity, and devastating impact on local banking systems, it prompted only fairly modest reform proposals. And even those stalled the moment the world economy began to recover. But if and when a future crisis ever hits the center of the world economy, the United States, motivation for fundamental IMS reform may be much stronger.

3) Wie schätzen Sie a. die Sinnhaftigkeit und b. die Durchsetzbarkeit regionaler Zielzonensysteme (etwa nach dem Muster des Europäischen Währungssystems 1978 bis 1998) ein?

Regional target-zone system for exchange rates make a lot of sense, since stable exchange rates provide for a better investment climate and better policy coordination. This is especially true for regions composed of national economies with strong intra-regional ties in terms of trade and investment flows. For instance, the European Monetary System (1979-1999) was absolutely necessary as a way for the EC currencies to float together against the US-dollar. Had such a system not been put into place, then the German mark would likely have risen (or fallen) too much against the dollar, certainly more than the other European currencies because of the strong flows between dollar and mark. And in that case there would have been unwelcome (and unjustified) changes in relative exchange rates within Europe which would have put the entire European integration project at risk. This was clearly evident during the period of the "snake" (1972-79), the predecessor to the EMS, when Britain, France, and Italy let their currencies float quite freely against the mark. Their efforts to make their industries more competitive through repeated devaluations constituted a form of monetary protectionism which undermined intra-European trade liberalization.

The EMS proved a success, not least because it encouraged nominal convergence (of interest rates and inflation rates in particular) among participating member nations. It also encouraged a convergence in policy-making, even though that convergence was perhaps excessively dominated by the policy priorities and performance standards of the Germans. With this convergence, a matter of significant macro-economic policy coordination among EMS members, came greater underlying exchange-rate stability, as manifest by the reduction in the number of exchange-rate adjustments after 1983 and a corresponding decline in the number of speculative attacks on specific exchange rates in the EMS. It certainly helped to have set up an intervention fund, the European Monetary Cooperation Fund, with which to counteract such attacks. I also liked the idea

of having a supranational monetary unit, the European Currency Unit (ECU), as the valuation anchor for the respective exchange rates withing the EMS. Calculated on the basis of a weighted basket of participating currencies, the ECU represented a benchmark average with regard to which interest-rate or exchange-rate deviations of individual currencies would be automatically smaller than when those differentials are measured relative to each other. It also helped that the EMS had built in a certain symmetry in adjustment burdens between countries with devaluing currencies and countries with appreciating currencies.

Generally speaking, regional target zones for exchange rates make sense for Europe and other regions of growing economic integration among neighboring countries, such as the CFA zone in Western Africa, the Mercosur area in Latin America, or the CIS countries composing the former Soviet Union. These regions do not have to be actually optimal currency areas, as defined by Robert Mundell, to qualify for a regime of fixed exchange rates or even a single currency. Not even the EU is an optimal currency area, given the limited mobility of labor across borders within that zone and the fact of external shocks possibly not impacting in symmetrical fashion across the region. The collapse of the Soviet Union, for example, had a dramatically stronger effect on Finland than on Portugal. Much weaker conditions of integration than those implied by Mundell's concept of optimal currency area suffice to warrant consideration of regional target-zone regimes. If they are set up like the EMS was, with provisions for joint pooling of reserves for exchange-rate management, symmetric adjustments, and macroeconomic policy coordination, such regional target-zone regimes have a good chance to succeed. The only practical (and essentially political) problem with such regimes is that they tend to be dominated by one leader whose policies and economic performance set the standard for others to follow. Germany's tough anti-inflation stance throughout the 1980s forced other countries in the EMS to keep their interest rates high and impose fiscal austerity even in the face of double-digit unemployment and slow growth.

The problem with any type of fixed-rate regime is that it typically fails to adjust exchange rates soon enough. There is a built-in inertia to maintain prevailing exchange rates for as long as possible even though the underlying relative positions of countries participating in such a regime may have already changed significantly. This was true for the postwar Bretton Woods system as it was for the EMS, and in each case this institutional resistance to appropriate adjustments created in the end violent crises forcing belated adjustments which went too far in the other direction. Neither in the crisis of Bretton Woods (1971-73) nor in the crisis of the EMS (1992/93) was it possible to sustain the exchange-rate regime as originally composed. One way to deal with this problem is to provide objective criteria for the timing and extent of exchange-rate adjustments which the members of the target-zone regime enforce consensually. This would entail specifying macroeconomic performance criteria for each member country (e.g. growth rates, inflation rates, interest rates, balance of payments).

Such adjustment guidelines would also improve the chances for a much more ambitious target-zone regime on a global level which would tie together the world's key currencies - the dollar, the euro, the yen, perhaps also the pound and the Swiss franc. As we have seen with the experience regarding the Plaza Agreement of February 1987, effective macroeconomic policy coordination is essential for the effectiveness of target-zone regimes. The G-7 initiative in 1987 ultimately has failed, because neither the US, nor the EU, and certainly not Japan have been willing to adjust their monetary and fiscal policies accordingly towards better convergence. The big powers are still stuck in an anachronistic world of national sovereignty and unilateral policy making. While we have seen in recent years better policy making (e.g. the Fed's willingness to let the US economy grow fast, Europe's struggle with meeting the convergence criteria of the EMU and the stability pact, Japan's repeated deficit-spending initiatives to get out of recession), the challenge of coordination now goes beyond fiscal and monetary policies towards structural reforms concerning financial institutions, public utilities (e.g. telecommunications), old-age protection systems, and so forth.

Change in that direction of reviving the 1987 target-zone experiment will in my opinion only come about in the aftermath of a new crisis centered on the US-dollar. The dollar has maintained its relative strength, even to the point of persistent overvaluation, because of strong capital flows from the rest of the world into US securities. Given the extremely low savings rate in the US, the US economy can only maintain its very high growth rates if foreign savings are used to fund its investment boom. But in the process the US has accumulated a $450 billion current-account deficit. This gap will start to play a greater role towards pushing the dollar down when two simultaneous developments kick in - changes in fiscal policy (no matter whether Bush or Gore wins) which will start to eat up the projected US budget surplus, and a reversal of the wealth effect when the stock-market boom in the US ends (which it is about to do). While these two forces may cancel each other out in terms of their effects on US savings, they will erode the attractiveness of US securities for foreigners - and this reversal in global capital flows may provide a rude shock to the dollar. Once the dollar starts declining, its fall can be quite significant which in turn might trigger a recession in the United States (because to the feedback effects between declining exchange rates and declining stock prices). The US will only consider global reforms if faced with such a crisis.

4) Halten Sie es für sinnvoll, das Tempo und Volumen des international Devisenhandels zu beschränken? Wenn ja, welche Instrumente sehen Sie hierfür als geeignet an (Tobinsteuer, Bardepotpflicht, administrative Kapitalverkehrskontrollen o. a.)?

In light of what happened in East Asia, Russia, and Latin America between 1997 and 1999, it seems clear that short-term capital flows across the globe have the potential of causing major disruption to the world economy when they suddenly reverse. As long as market expectations are pretty well spread, the system is fairly stable due to a balance between demand and supply of short-term financial instruments. But such expectations tend to follow a cyclical pattern and in the process are usually inclined towards becoming homogenous - first in the context of a generalized euphoria encouraging excessive risk-taking and then, when the euphoria hits a wall amidst signs of trouble from overextension, a generalized panic with everyone running to the exit doors at the same time. We also have to be aware that these short-term "hot money" flows are often highly leveraged to multiply rates of return (on a smaller capital base). The debt involved in building such a leverage effect only reinforces panic selling in a crisis, because the securities acting as collateral backing this debt get devalued to the point where they have to be dumped. At that point there are likely to be some large institutions which have taken excessively risky positions which are forced to liquidate, providing in this way a brutal shock to already panicky markets - a very dangerous situation (as evidenced by the failure of America's largest hedge fund, Long Term Capital Management, in September 1998 and its spectacular rescue under the auspices of the Fed).

More generally, the key problem with today's "hot money" flows is a fundamental contradiction between the speed of these flows and the considerably slower ability of societies to change their structures in accommodation of these flows. Moreover, there is something dreadfully wrong with our economic system when trillions of dollars flow around the globe each day trying to preserve themselves in their liquidity with lots of

paper profits ("capital gains") while three quarters of the world is suffocating under the burden of long-term debt and long-term investment funds are hard to come by. It takes perhaps $10 committed to short-term credit pyramids (including all sorts of derivatives) to bring forth $1 in productive investment spending. As a result there is an intense maturity mismatch between the short-term liabilities of many countries depending on such "hot money" funds and their long-term assets, a mismatch that will paralyze local banking systems in any situation of capital-flow reversals and throw those national economies into deep recession - as evidenced in the 1997-99 crisis.

We should also understand that the "hot money" flows project political power, one that is likely to grow as more and more Americans and Europeans are investing in mutual funds and pension funds which are the principal vehicles of that "hot money." And this political power forces governments to pursue a policy agenda which may not be in the best interests of their citizens at large - high "real" interest rates, limitations on deficit-spending, deregulation of business, privatization of public-sector enterprises, and tax reform favoring wealthy investors. Even in Europe governments have found that they are no longer in control of their policy destiny, a situation that is much more critical in the developing world.

The idea of restricting excessive and volatile "hot money" flows through regulatory restrictions has therefore merit inasmuch as such restrictions slow down and reduce the volume of those flows. There is always the conservative counterargument that such restrictions erode the liquidity in financial markets and therefore make those markets less efficient. In my view there is too much liquidity and too much efficiency in those markets to begin with. Moreover, it is precisely the volatility of those markets which encourages everyone to speculate and/or to hedge. If those markets can be made more stable, there is less incentive for speculation and hedging, thus a decline in the demand for "hot money."

The problem with such restrictions is that they have to be global in nature in order to match the global dimension of “hot money.” Unilateral measures, such as recently enacted with some degree of success in Chile or Malaysia, can only work temporarily. Eventually any such unilateral restrictions will deprive the country putting those into effect of necessary access to international financial markets. If you want to have durable controls, they have to be enacted and administered globally, a complex task. Among the possible measures in this direction I favor the Tobin Tax. Since this would be a transaction tax, it would hit disproportionately the short-term movements of capital (i.e. “hot money”) while barely burdening the longer-term activities of trade and direct investments which tend to be more productive in nature. Such a tax would also give the world community a lot of revenues which could be used for a variety of very useful global projects - debt forgiveness for the poorest nations, environmental initiatives (against global warming, deforestation, etc.), and/or social safety nets in support of labor- and environmental-protection codes which should accompany the creation of a new fair-trade regime.

Of course, there are other measures to consider besides the Tobin Tax. Mandatory reserve requirements for short-term capital flows across borders serve as a sort of tax and make them less attractive. Administrative capital and exchange controls are in this context probably less useful, given the highly sophisticated and fully privatized payments-system infrastructure of “hot money” (e.g. SWIFT, CHIPS). I believe financial institutions would not have great difficulty finding ways to circumvent such adminstrative controls, even ones that are put into place on a global scale. For such controls to work, one would have to replace SWIFT and CHIPS with a public payments system controlled by an international monetary authority. More realistic are in my view new regulatory mechanisms pertaining to financial institutions engaged in “hot money” flows. I would certainly want to introduce new disclosure, accounting, and regulatory guidelines for financial derivatives to make them more transparent to all parties involved. It would help greatly to limit the leverage involved in such contracts through margin requirements that would require a fairly significant portion of a contract’s value

to be financed with one's own capital. Finally, taking my cue from the 1988 Basle Accord imposing a uniform minimum risk-adjusted capital-asset ratio on the operations of transnational banks (the socalled "Cooke Ratio"), I would move towards a new regime of reserve requirements based on the riskiness of assets. So far reserve requirements have been used against liabilities and confined to banks. Such requirements should be focused instead on assets, which is where the "hot money" is, and be extended to other financial institutions, notably mutual funds and hedge funds.

In conclusion, there is much to be reformed in the international monetary system, as currently constituted. In my opinion the Europeans will have to play a crucial role in pushing forth such a reform agenda. They are powerful, uniting as a bloc to challenge the dominance of the US, and their Third Way politicians (Schröder, Blair, Jospin, et alii) have to contextualize new types of reforms for the "New Economy." It also makes sense to have a globalist vision of policy reform, not least in contradistinction to both the rather isolationist US propensities and the excessively ideological belief in the "free market" pushed by the "Washington Consensus."