

Economic ministers gather in Washington

Confronting the mounting global financial crisis

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When the finance ministers and leading economic officials of the 22 major capitalist countries gather at the Willard Hotel in Washington this Thursday, they will have more on their agenda than the immediate financial crisis in Asia.

The meeting has been called to initiate discussions on a “new architecture” for the international banking and financial system, amid fears that the Mexico crisis of 1994-95 and the Asian meltdown of 1997-98 are only the first signs of bigger storms to come. In the immediate aftermath of the initial Asian currency crisis, US President Clinton dismissed the turbulence as a “glitch.” Others, however, have now recognised that it is anything but that.

According to one of the leading officials in Japan’s Ministry of Finance, Dr Eisuke Sakakibara, what is taking place is “a crisis of global capitalism.” His views are shared, at least privately, by others.

Greenspan’s fear

In a recent address to a bankers’ conference in Miami, the normally restrained head of the US Federal Reserve Board, Alan Greenspan, described the situation which emerged in Asian markets as one based on a “visceral, engulfing fear.” He indicated that the state of confidence necessary for the running of an economy had been “torn asunder.”

Pointing to the wider implications of the Asian crisis, he said that while the newly evolved international financial system had brought about a massive increase in global capital flows, it had also “facilitated the transmission of financial disturbances far more effectively than before. The crisis in Mexico several years ago was the first such episode associated with our new high-tech international financial system. The current Asian crisis is the second.”

He told the assembled bankers that “hopefully before we run into crisis number three—and there will be a crisis number three—we’ll have sufficient preventative measures in place to either fend it off, or, if it occurs, to assuage its severity.”

Greenspan concluded his remarks by posing the question as to how these “critical tendencies towards disequilibrium and vicious cycles” could be addressed in the future, declaring that “the architecture of the international financial system will need to be thoroughly reviewed and altered as necessary to fit the needs of the new global environment.”

But while Greenspan and other officials will point to the major problems confronting the global capital and money markets when they meet on Thursday, their efforts to effect a solution are faced with insurmountable contradictions, as an examination of the historical evolution of the

international financial system will make clear.

The Bretton Woods system

The existing “international financial architecture” was devised at the conference of 44 nations held at Bretton Woods, New Hampshire in 1944. It was convened by the United States and Britain to set up a new global financial order to prevent a repeat of the depression and financial crises which had ripped through the world capitalist economy in the inter-war period.

The designers of the new system—the chief adviser to the British government, John Maynard Keynes, and the US Treasury official, Harry Dexter White—set out to meet two goals. In order to ensure economic growth, the protectionist barriers that had led to the unprecedented two-thirds contraction of world trade in the 1930s had to be progressively dismantled and the international market reestablished. However, while there should be free movement of goods, tight controls should be maintained over the international movements of capital and finance.

These two aims were embodied in the so-called Bretton Woods system. Trade was facilitated through the lowering of tariffs under GATT (General Agreement on Tariffs and Trade), while a stable international monetary system was based on the supremacy of the US dollar. Under the agreement, the currencies of the major capitalist countries were fixed in terms of the US dollar, which functioned as an international currency, backed by gold at the rate of \$35 per ounce.

At the same time, in order to prevent competitive currency devaluations and violent interest rate movements, countries experiencing short-term balance of payments and currency difficulties were assisted with finance from the International Monetary Fund, while the World Bank was set up to organise long-term capital movements to poorer nations.

The prevailing atmosphere at Bretton Woods was a far cry from the “free market” ideology which dominates financial and government circles today. In fact, the architects of the post-war financial order believed that the unfettered operation of the market, especially the international movement of finance capital, had precipitated the crises of the 1920s and 1930s. They sought to use the combined power of the capitalist states to regulate the inherent drive of capital to leap across national borders.

As US Treasury Secretary Henry Morgenthau told the conference, the aim of the agreement was to “drive the usurious moneylenders from the temple of international finance.” And in the words of Keynes: “Not merely as a feature of the transition but as a permanent arrangement, the plan accords every member government the explicit right to control all

capital movements. What used to be heresy is now endorsed as orthodoxy.”

Behind the overturn of the previous free-market program was the fear of social revolution. Keynes and White insisted that the social welfare and full employment programs being set in place by all the major capitalist governments as a concession to the working class would break apart, leading to social upheaval, unless mechanisms were put in place to regulate the international movement of money and capital.

The collapse of Bretton Woods

The cornerstone of the Bretton Woods system was the fixed currency exchange rates based on the US dollar, and it was here that the cracks first began to appear—a result of the fundamental contradiction on which the entire system was based.

While Bretton Woods was founded on the strength of the US dollar—its short supply vis a vis other major currencies—the provision of increased liquidity to finance the growing volume of trade and other international transactions required a continuous outflow of dollars from the US, ultimately undermining the US currency.

By the end of the 1960s, the mass of dollars circulating in the rest of the world began to outstrip the reserves of gold held by the US to back it. In August 1971, with the emergence of a US trade deficit for the first time since the war, President Nixon removed the gold backing from the US dollar. Attempts were made over the next 18 months to maintain the fixed exchange rate system, but it finally collapsed in February 1973.

The ending of the Bretton Woods monetary system and the establishment of currency floats, in which the exchange relations between major currencies were determined on the market, was to have far-reaching consequences. As the value of currencies began to be determined in the international market, the maintenance of restrictions on international capital flows, either by governments or central banks, became increasingly inviable.

If, for example, a government sought to intervene against the market to prevent capital movements, the pressure of market demands would simply be reflected in sharp movements of currency values.

Faced with the impossibility of maintaining a partially regulated system, the major capitalist governments were forced to progressively dismantle controls on both currency and capital flows during the 1980s. As a consequence, semi-independent national markets have now been replaced by a global market in which finance capital, whatever its particular national origin, moves around the world in search of the best conditions for profit.

The return of global disorder

But the establishment of an unregulated global financial market has raised all of the fundamental issues which confronted the architects of the Bretton Woods system. The increasingly rapid movement of finance capital around the world brings with it economic and social disorder.

Figures now being released on the Asian crisis make this clear. According to the Institute of International Finance, which represents some 285 international banks and financial institutions, the five most affected countries experienced short-term capital inflows of \$14 billion in the first nine months of last year, followed by a massive \$33 billion outflow in the last three months.

This violent turnaround not only threatened the viability of Asian banks and financial institutions but, according to a recent report by the Bank for International Settlements, could have sparked a “systemic” crisis of the global financial system. The threat which hangs over the international financial system is that when another crisis erupts—and, as Greenspan acknowledges, there is certain to be a next time—it will bring about such a financial unraveling.

The central item of discussion at the G-22 Willard Group will be the establishment of some form of international regulator system. But, however much the necessity for such global regulation is recognised in the abstract, there are insurmountable barriers to its implementation.

In a recent article published in the London-based *Financial Times*, Massachusetts Institute of Technology economics professor Paul Krugman warned that the move from nationally-regulated financial systems to a deregulated global financial system created the conditions for a return of panic attacks on financial markets.

“Put it this way: we have in effect moved from national to global financial markets without creating a corresponding global version of national regulation or national safety nets. If politics were no constraint, the solution would be obvious: recreate at a global level the safeguards that used to work at a national level.

“This would mean a sort of super-International Monetary Fund, with the huge resources needed to act as a lender of last resort, and with extensive direct regulatory powers over the banks of member countries. And while we are at it, let us have cold fusion, a cure for the common cold, and brotherly love among all men.” (*Financial Times*, April 9, 1998)

In other words, however necessary a system of international regulation might be, it is impossible to implement because of the conflicting interests of the major capitalist countries.

Irreconcilable antagonisms

Those opposed agendas will be not far below the surface of discussion during the Willard Hotel gathering. US Treasury Secretary Robert Rubin made it clear in a major address to the Brookings Institute this week that the US favours letting the banks incur losses, rather than being continually bailed out by the IMF. Undoubtedly this view reflects the fact that the biggest losers in the Asian crisis will be the Japanese banks.

The European powers on the other hand, still smarting from the roughshod treatment they received three years ago when the Clinton administration used IMF funds to bail out American banks caught in the Mexican crisis, will be looking for an expanded voice in IMF and international financial affairs with the coming of the single European currency, the euro, at the start of 1999.

The euro is aimed not only at European integration, but at establishing an alternative world currency to the US dollar. But even as its architects strive to extend its global reach, the single currency itself could well be the subject of a financial crisis. The latest edition of the financial magazine *Euromoney* devoted its cover story to warnings of a disaster that could hit the euro.

“In 1912,” its report began, “shipbuilders Harland & Wolff had somehow convinced the public that their latest creation, the Titanic, was unsinkable. Today, the architects of European economic and monetary union (EMU) are spreading the same propaganda about the SS Euro, scorning any thought of lifeboats or muster stations.”

The dangers have arisen from the fact that while the Maastricht Treaty set the ground rules for entry to the EMU, there were no regulations covering the exit of one or more countries.

The article went on to list some 10 “icebergs” which could sink the

project, including a speculative run on European currencies, dislocation of clearance and payments systems, mass unemployment and Europe-wide recession, expulsion of a country which fails to meet the single currency requirements, and the impotence of the European Central Bank. The magazine's editorial warned that the 11 countries signed up for the single currency "now appear to be sleep-walking into a theatre potentially as apocalyptic as the Great War."

While the statements issued at the conclusion of the G-22 meeting will undoubtedly consist of upbeat endorsements of the efficacy of the market and confident projections of economic growth, the convening of the Willard conference itself is an expression of the fact that the central contradiction of world capitalism in the twentieth century—that between the development of world economy and the division of the world into rival nation states—is emerging once again.

That contradiction, which has already given rise to two world wars, cannot be resolved by the capitalist governments, even when the increasingly dangerous monetary storms force them to recognise its existence. The harmonious development of the productive forces, which have well and truly burst through the confines of the nation-state, can only be assured through the overthrow of capitalist property relations by the international working class and the establishment of a planned socialist world economy.



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