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Reconstructing a new financial structure

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GOING by the line propagated by much of the international media, the world has put behind itself the spectre of global deflation - a fear spawned by the East Asia crisis in mid-1997 and heightened by the Latin American and Russian crises in 1998.

The mood in the international economy is one of smug complacency and even self-congratulatory as the relative stability of financial markets in the past year evokes perceptions that global capitalism has, again, managed its own contradictions quite successfully.

"This is utter nonsense, the crisis is not over," declares Charles Santiago from Stamford Centre of Economic and Social Research.

His contention: The crisis-ridden countries have not debunked the Asian economic growth model, centred on trade and financial liberalisation which led to the crisis in the first place; socio-political change in these countries are not over; and the present initiatives taken by the G-7 to reconstruct a new monetary architecture do not solve the underlying causes of the crisis.

Institute of Strategic and International Studies' Dr Zainal Aznam Yusof is equally skeptical of the commitment and will of G-7 or the North-led grouping to structurally change the global monetary system.

"There must be a Big Bang approach rather than the present little, whimpering efforts. What else are we waiting for?"

A cursory comparison between the response to the Mexico crisis of 1994 and the present response shows that the two do not differ substantially nor go far enough to prevent a recurrence:

A pledge to renew and revitalise the International Monetary Fund and World Bank as cornerstones of a new architecture for the post-Cold War international monetary system (G-7 Summit at Halifax, Nova Scotia, June, 1995);

A greater surveillance on IMF member countries' macroeconomic policies and a pledge to boost its resources to cope with any future Mexico-like emergency - what managing director Michel Camdessus then described as "a crisis of a new kind, the first of the century" (IMF Interim Committee meeting at Washington, April 1995).

The present initiatives include the previous pledge to reform the IMF and World Bank; a greater surveillance and monitoring system through closer co-operation among financial regulators and the World Financial Stability Forum; a credit package, the Contingency Credit Line (a similar lending facility was stillborn in 1995) for countries in distress.

There were talks of regulating hedge funds but these dissipated in inaction. The G-7 summit at Cologne this June did not yield substantive action in altering the global monetary system.

As Santiago puts it: "The G-7 is merely concerned about demanding greater transparency, non-corruption and corporate governance from the crisis-ridden countries and the US in pressing Europe and Japan to double their efforts to suck in more goods from developing countries so that these countries can export their way to economic health."

In June, Lawrence Summers, the US' newly ensconced treasury secretary, had expressed worries that the US is still the world's "importer of last resort".

Many seem to agree with him but those who wax eloquent on the role played by the US economy as the only engine of growth in the current

international economic configuration should remember that this is also due to the inflow of savings into the US from the rest of the world.

The G-7's rejection of the proposed Asian Monetary Fund, an Asean currency and the proposal by Japan and Germany for a balanced currency band that includes yen, euro and dollar, shows it is more concerned in promoting further financial liberalisation rather than addressing the root causes of the crisis.

It wants the countries to behave like international corporations whose duty is only for stakeholders, who would be mainly the international investors, and not the citizenry.

As for hedge funds, most disappointing is the US' point of view which finds nothing wrong with it except for a little lack of transparency.

Even though the G-7 broadens the system-building process to include the active participation of the big banks and international investors which dominate the international capital market, their presence is irrelevant since there is active effort to validate their activities in the current form.

"The present measures do not strike at the key things that're wrong with the global system. There must be some control over the economic agents, the speculators and investment bankers who provide the money.

"Without a strong agreement to regulate the movement of short-term capital flows, there won't be any substantial progress.

"The thinking that speculation brings stability and one has to live with these bloodsucking vampires flies in the face of facts," says Zainal.

He adds that complacency has been embedded in the international system as to the severity of crises, consequences of systemic risks and the ineffectiveness of conventional approaches to the crises.

Many believe the worst is over. But the voluminous United Nations Department of Economic and Social Affairs' publication, entitled The World Economy in 1999 shows that in terms of real economic indicators, there is no evidence of recovery in the world economy and hence, the present financial stability is inherently fragile.

World trade in volume terms grew by about 3.5 per cent in 1998 - which is the smallest of increases this decade and less than half the rate in 1997.

This low rate of increase resulted from the almost five per cent decline in imports of developing countries and the 10 per cent import drop in Japan.

The UN estimates that in 1999 import levels will begin to recover, albeit slowly, with import volumes rising 2.5 per cent in developing countries and 0.25 per cent in Japan.

As has been constantly pointed out by Prime Minister Datuk Seri Dr Mahathir Mohamad, although crisis-ridden countries managed to stabilise their currencies, exchange rates for many have remained at values far below their pre-crisis levels.

This means a net loss of real income and hence purchasing power in these countries, already compounded by the declining unit values of their exports.

"The world can no longer be dependent on G-7. Asian nations should articulate a different position and solicit support from Europe.

"China, too, must ask itself how it can support the Asian cause. Roping China in is important as the US takes China more seriously than Asia.

"Geo-politically, Japan and Europe must re-align themselves.

Unfortunately, most European governments are pro-US.

"At the same time, Asian nations must articulate a growth model which is sustainable," asserts Santiago.

Zainal believes that what man does can be undone. But there is no

serious undertaking to reconstruct a new financial architecture.

Today's stability is hollow and is a prelude to yet another round of crisis in the future.

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