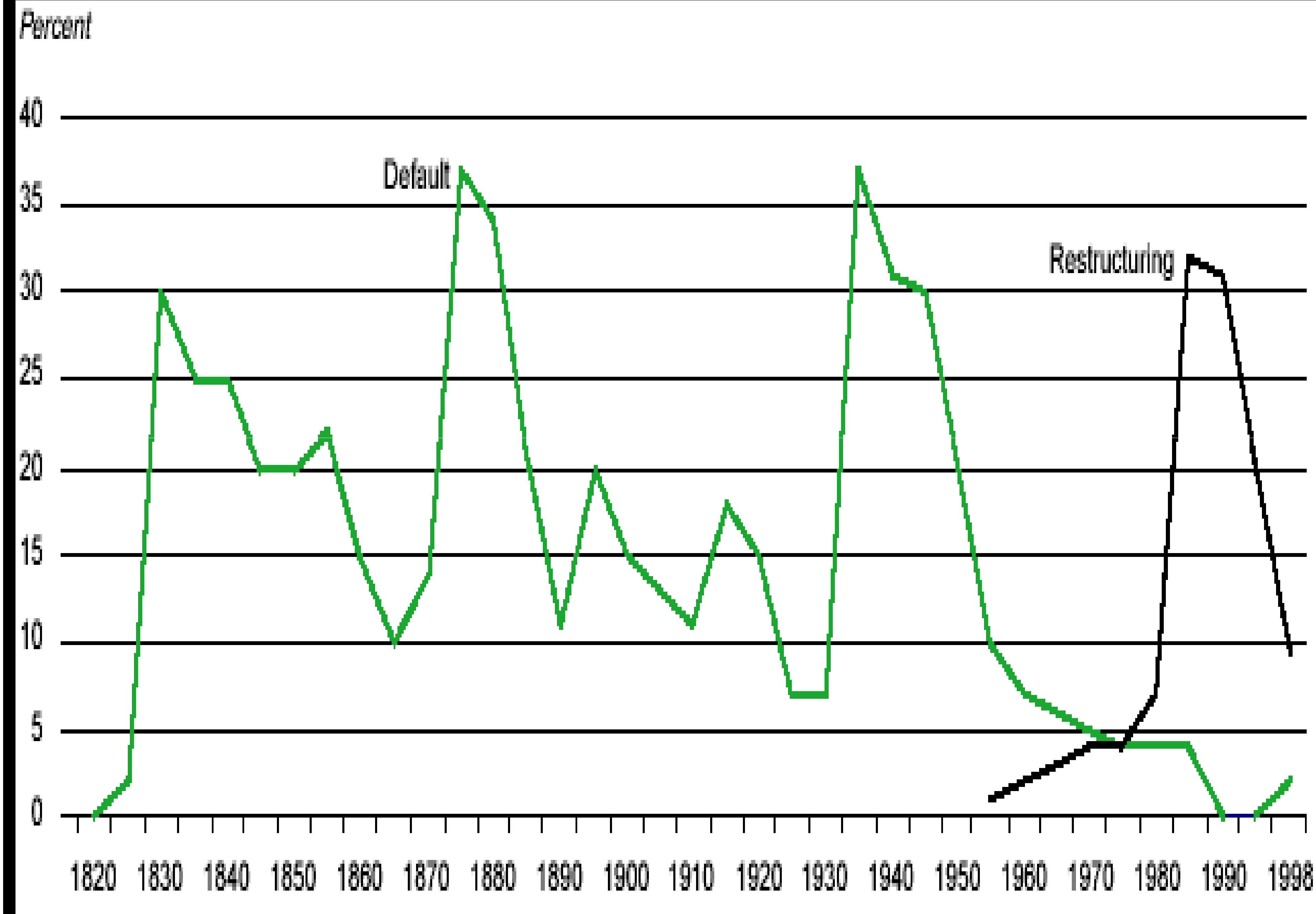
The International Financial System and the Need for a New International Financial Architecture

by Patrick Bond
Durban, South Africa
July 2011

Sovereign debt defaults, 1820-1999: percent of national states

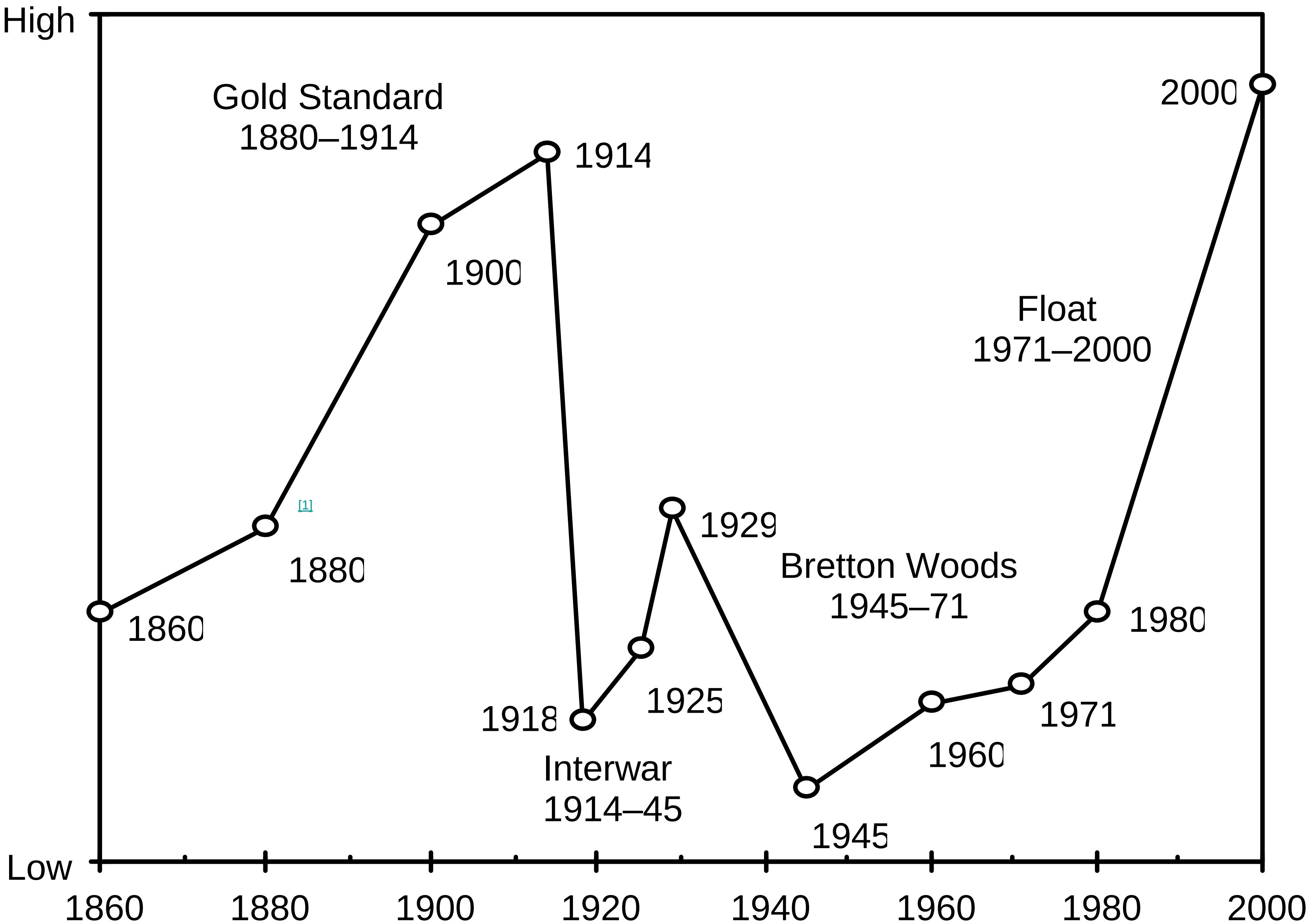


Evolution of international financial architectures

Date	System	Reserve Asset(s)	Leader(s)
1803-1873	Bimetallism	Gold & Silver	France
1873-1914	Gold Standard	Gold and £	Britain
1915-1924	Anchored $ St.	Gold and $	US
1924-1933	Gold Standard	Gold,$ and £	US, UK, France
1934-1971	Anchored $ St.	Gold and $	US, G-10
1971-1973	Dollar Standard	$	US
1973-1985	Flex. Ex. Rates	$, DM, £,	US, FRG
1985-1999	Man. Ex. Rates	$, DM, ¥	US
1999-2010	Dollar and Euro	$, €, ¥, £	US EMU
2010-?	Currency Areas	$. €, ¥, C¥, £	US, EMU

Source: R. Mundell, 'Euro in a New International Financial Architecture', May 27, 2010, Joint EBF - ABA Conference: "Inter-Regional Banking Cooperation for Solid Financial Future" in Baku, Azerbaijan

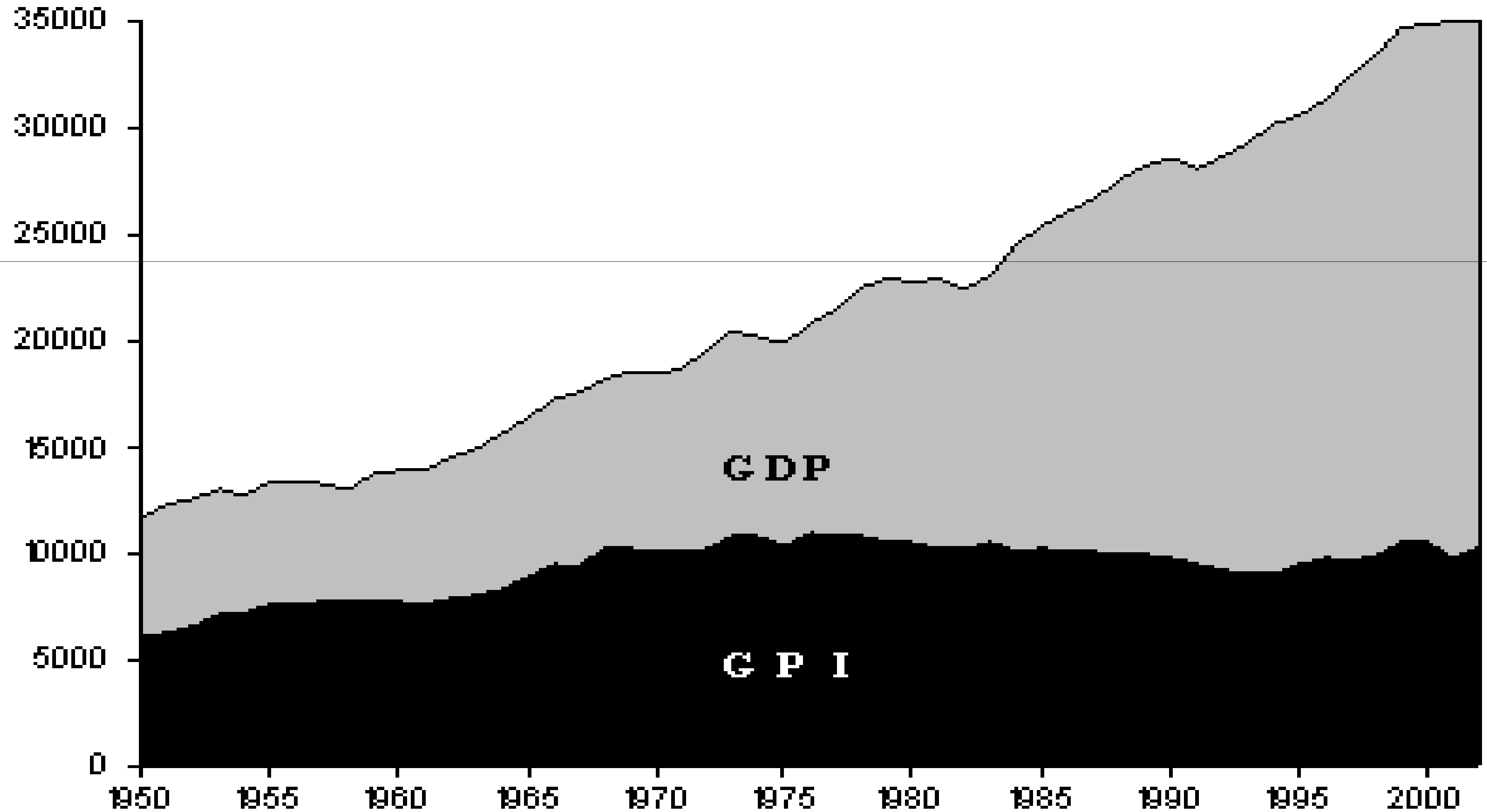
Degree of international financial integration



Source: Stiin Claessens and Maurcie Obstfelt

$DXY - Dollar Index (INDEX) - Daily OHLC Chart
Op:80.27, Hi:80.31, Lo:80.09, Cl:80.15
dollar volatility, 2000s
U.S. Dollar down over 33% since 2000
panic of late 2008
(c) Barchart.com
125.00
120.00
115.00
110.00
105.00
100.00
95.00
90.00
85.00
80.15
75.00
70.00
65.00
2001
2002
2003
2004
2005
2006
2007
2008
2009
2010

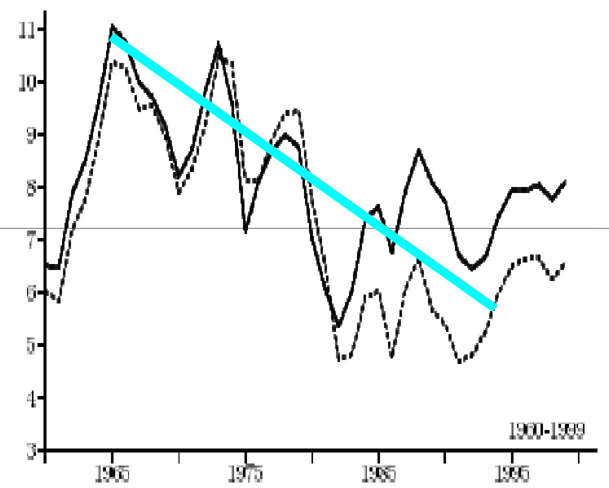
Dubious statistics:
Correcting the GDP bias (global)



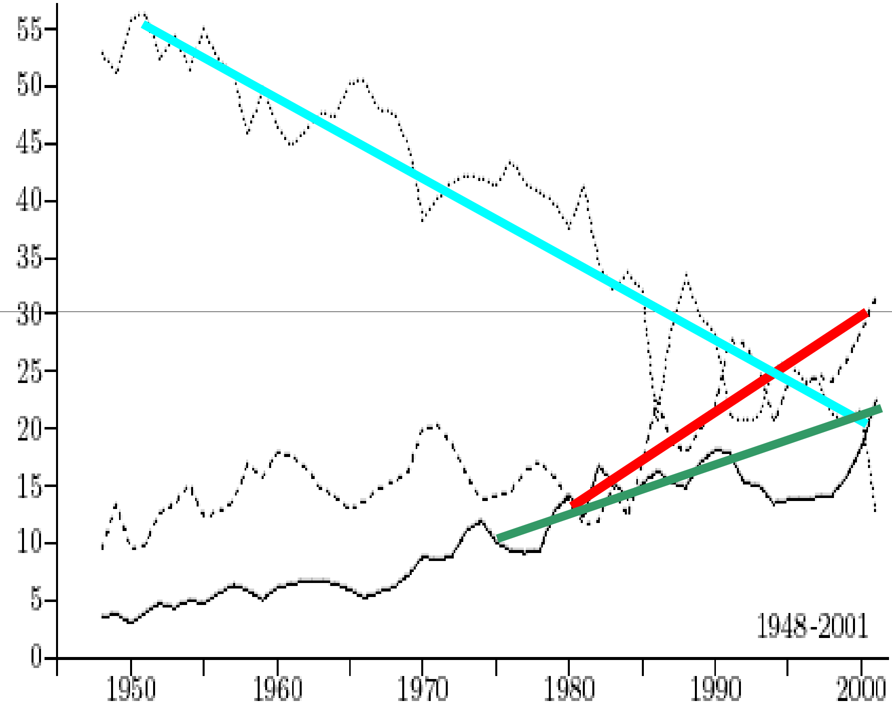
Source: redefiningprogress.org

root ‘overaccumulation’ process: source of declining US profits during globalisation/financialisation era

Figure 3 US nonfinancial corporations: Profit rates prior to the payment of real interest (——) and after (-----), %



In the first series, profits are equal to the net product minus the cost of labor, and business and profit taxes. They are divided by the net worth (total assets minus debt). For the second series, real interest is subtracted from profits, *i.e.*, interest minus a correction for the depreciation of debt resulting from inflation.



Rest of the world: (——); Financial sector: (-----); Manufacturing: (·········)

Profits are measured before profit taxes. The *rest of the world* corresponds to the excess of profits made on US investments abroad over the profits made by the rest of the world on foreign direct investment in the US. (These profits may remain in the country where the investment is made.) Trade, Contruction, Public Utilities, Transportation and Communications, and services are not represented.

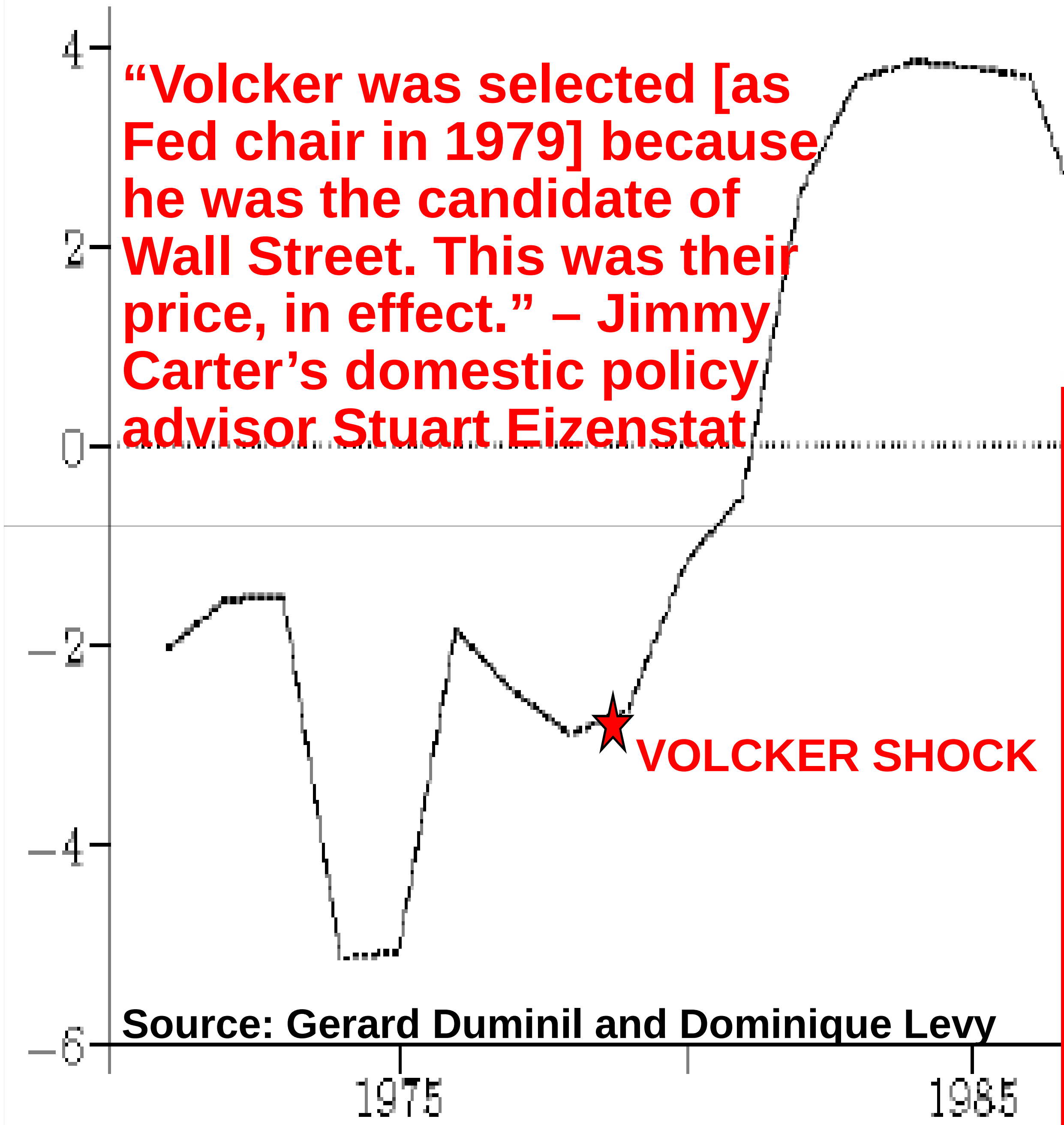
Source: NIPA (BEA).

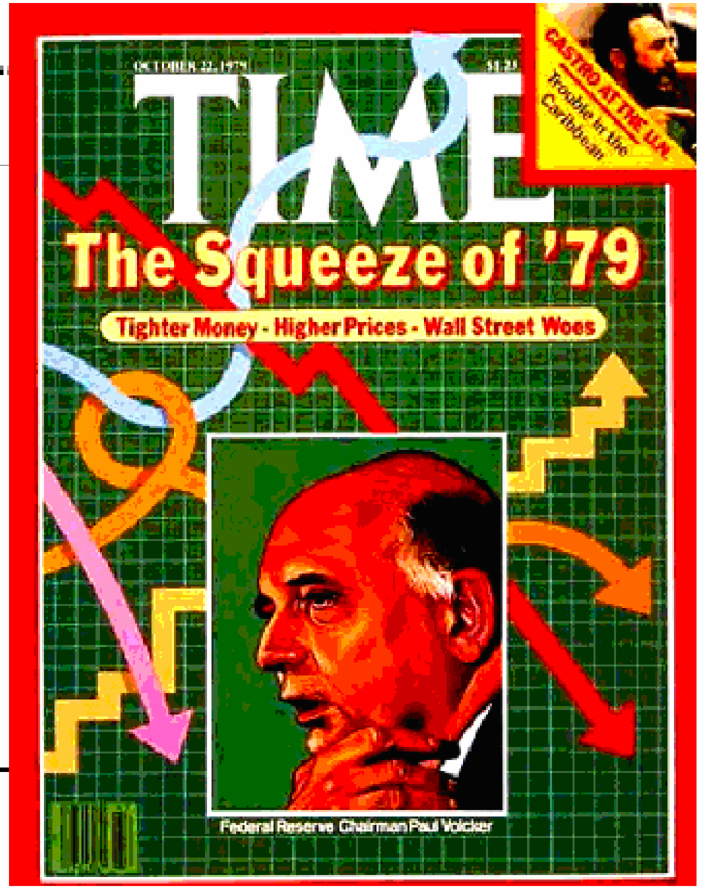
US corporate profits derived much less from manufacturing products;
much greater sources of profits came from abroad;
profits also came more from returns on financial assets.

Source: Gerard Dumenil and Dominique Levy

Real interest rate rise with Volcker as Federal Reserve chair

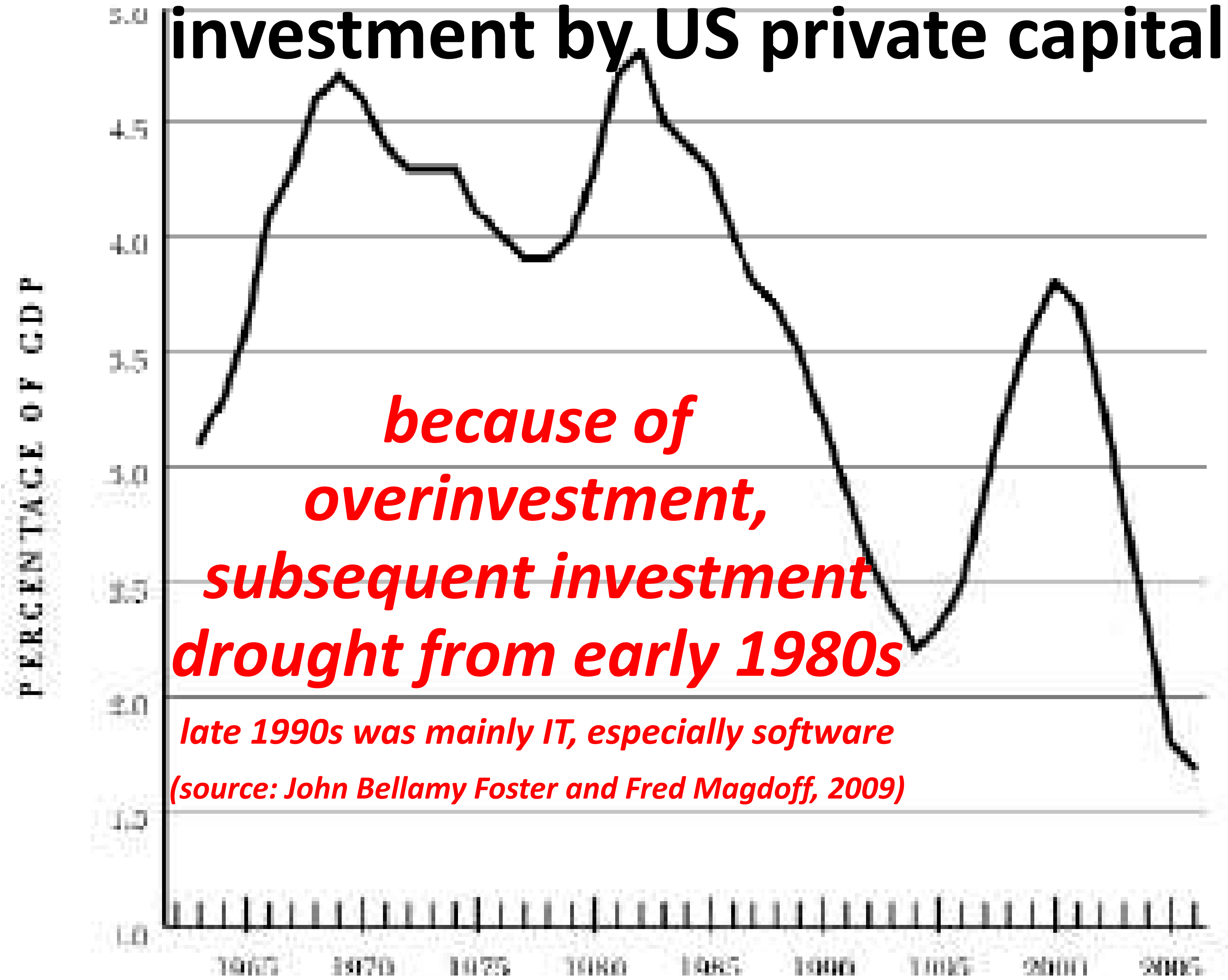
"Volcker was selected [as Fed chair in 1979] because he was the candidate of Wall Street. This was their price, in effect." – Jimmy Carter's domestic policy advisor Stuart Eizenstat





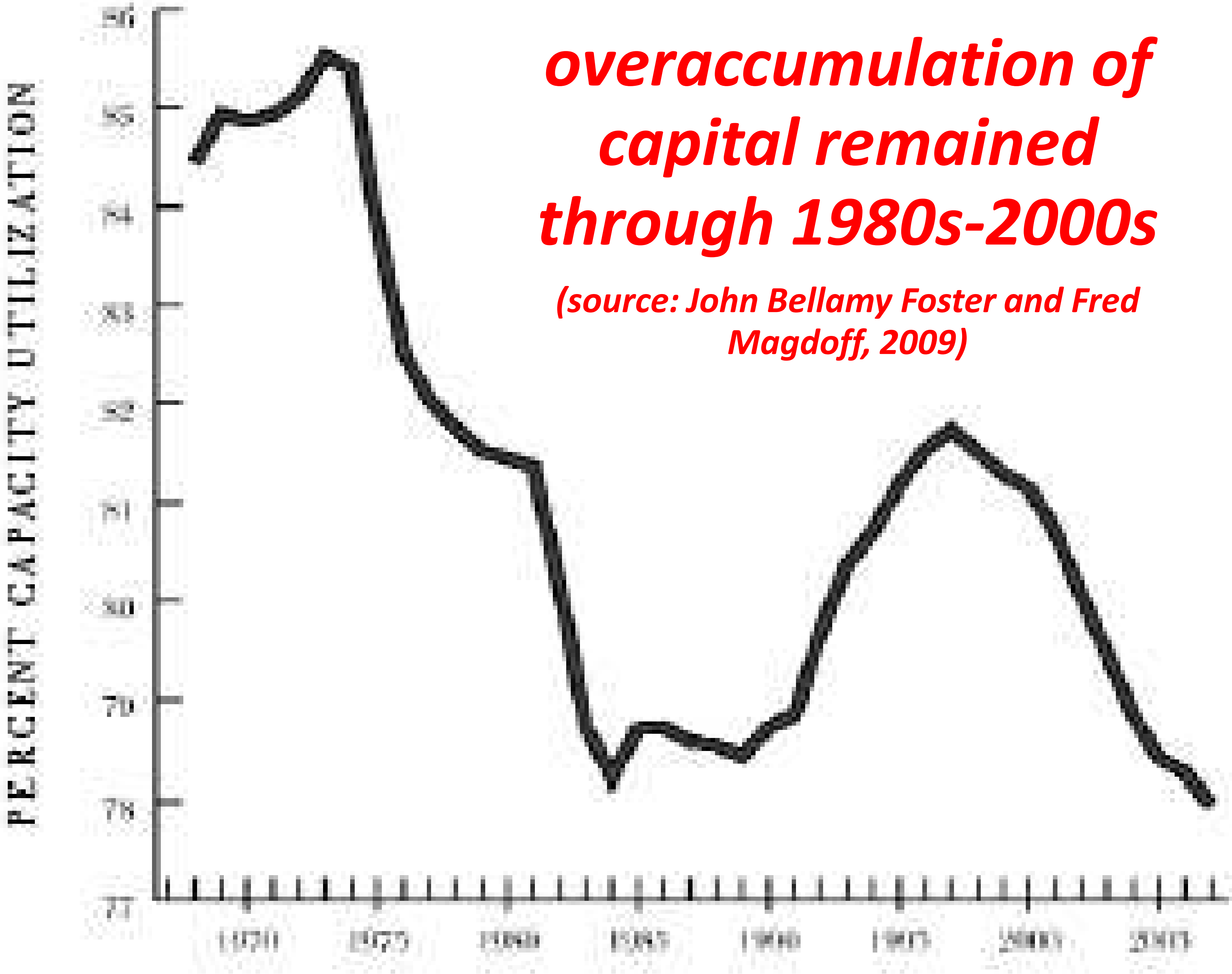
Source: Gerard Duminil and Dominique Levy

investment by US private capital



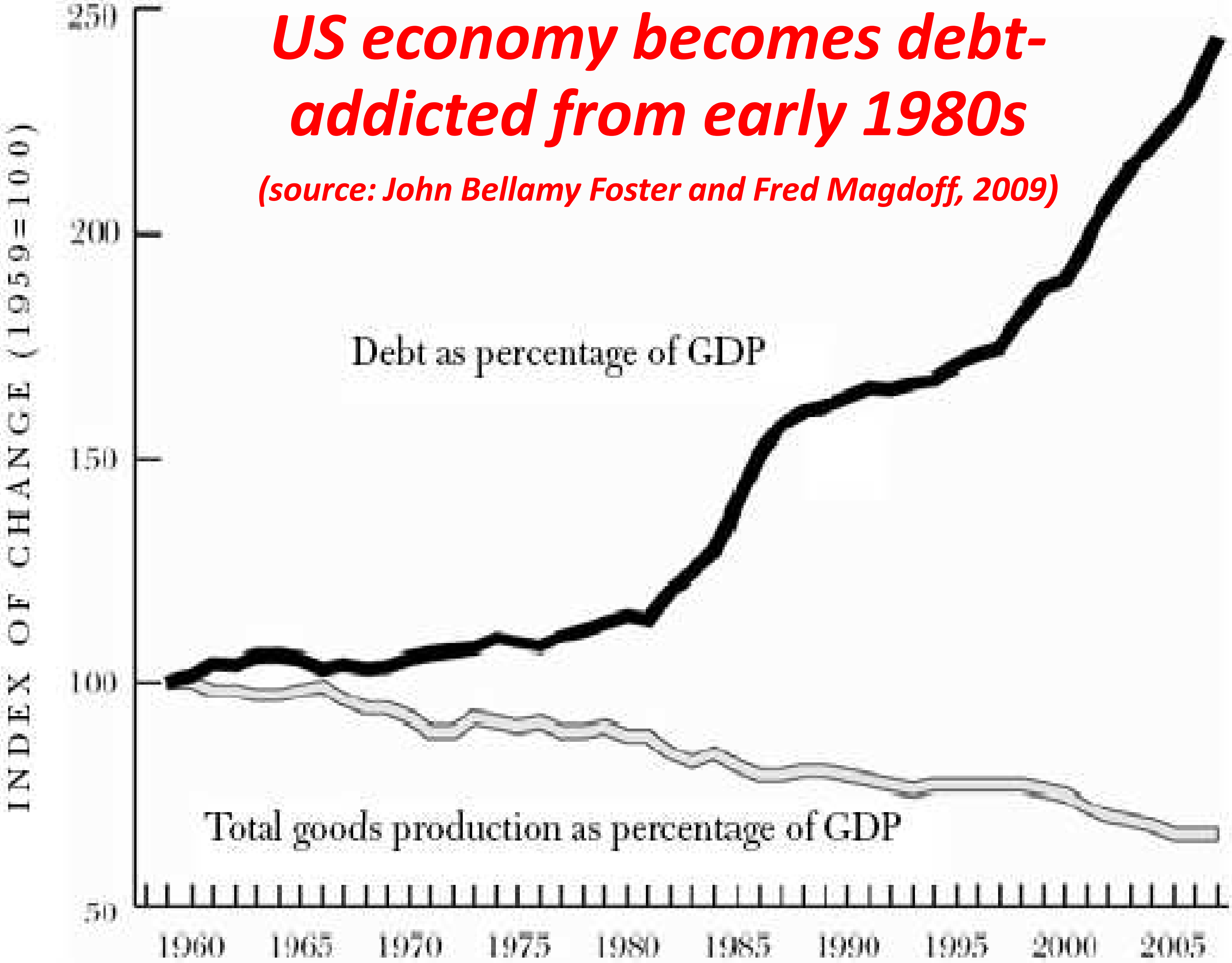
overaccumulation of capital remained through 1980s-2000s

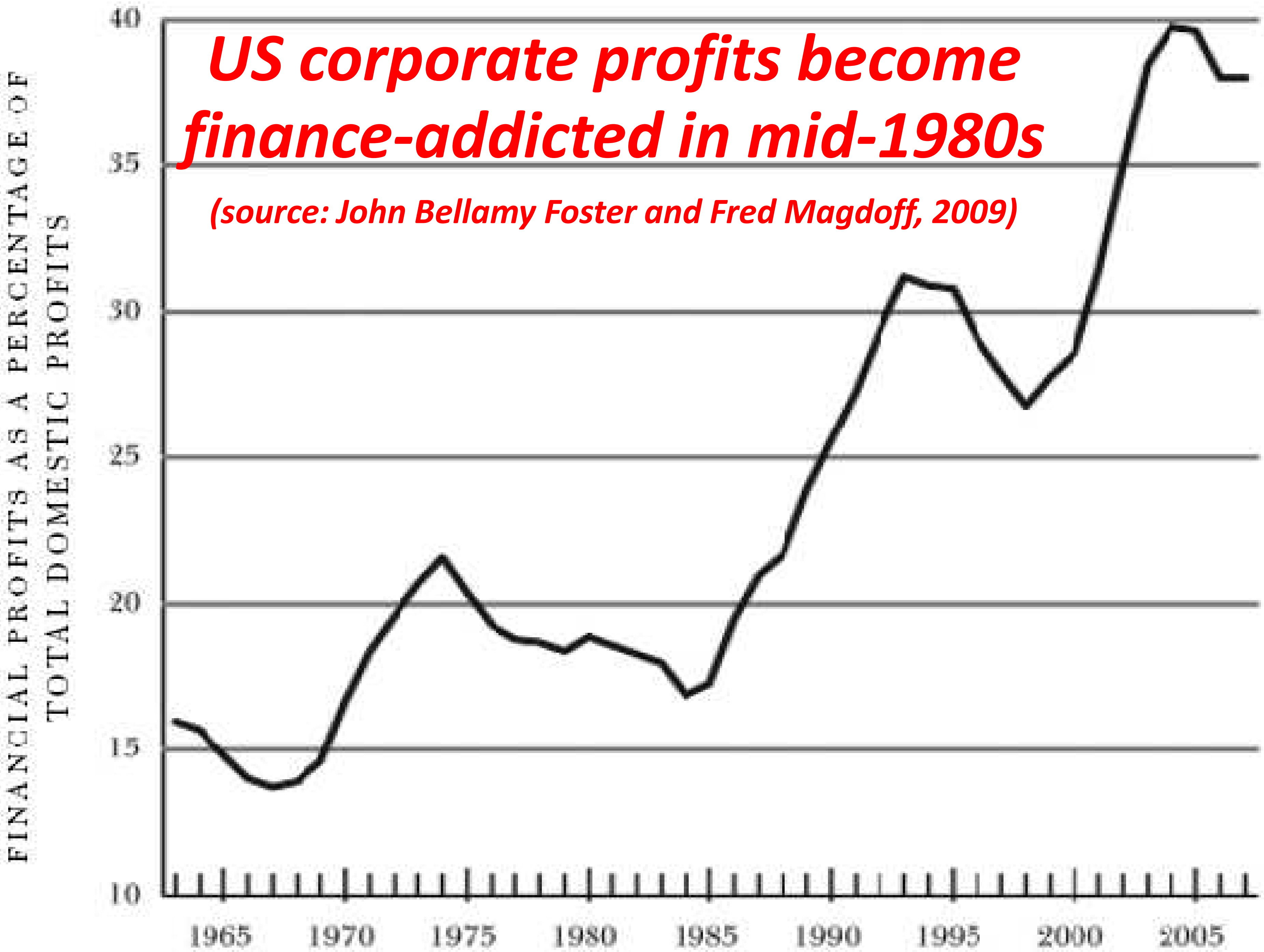
(source: John Bellamy Foster and Fred Magdoff, 2009)



US economy becomes debt-addicted from early 1980s

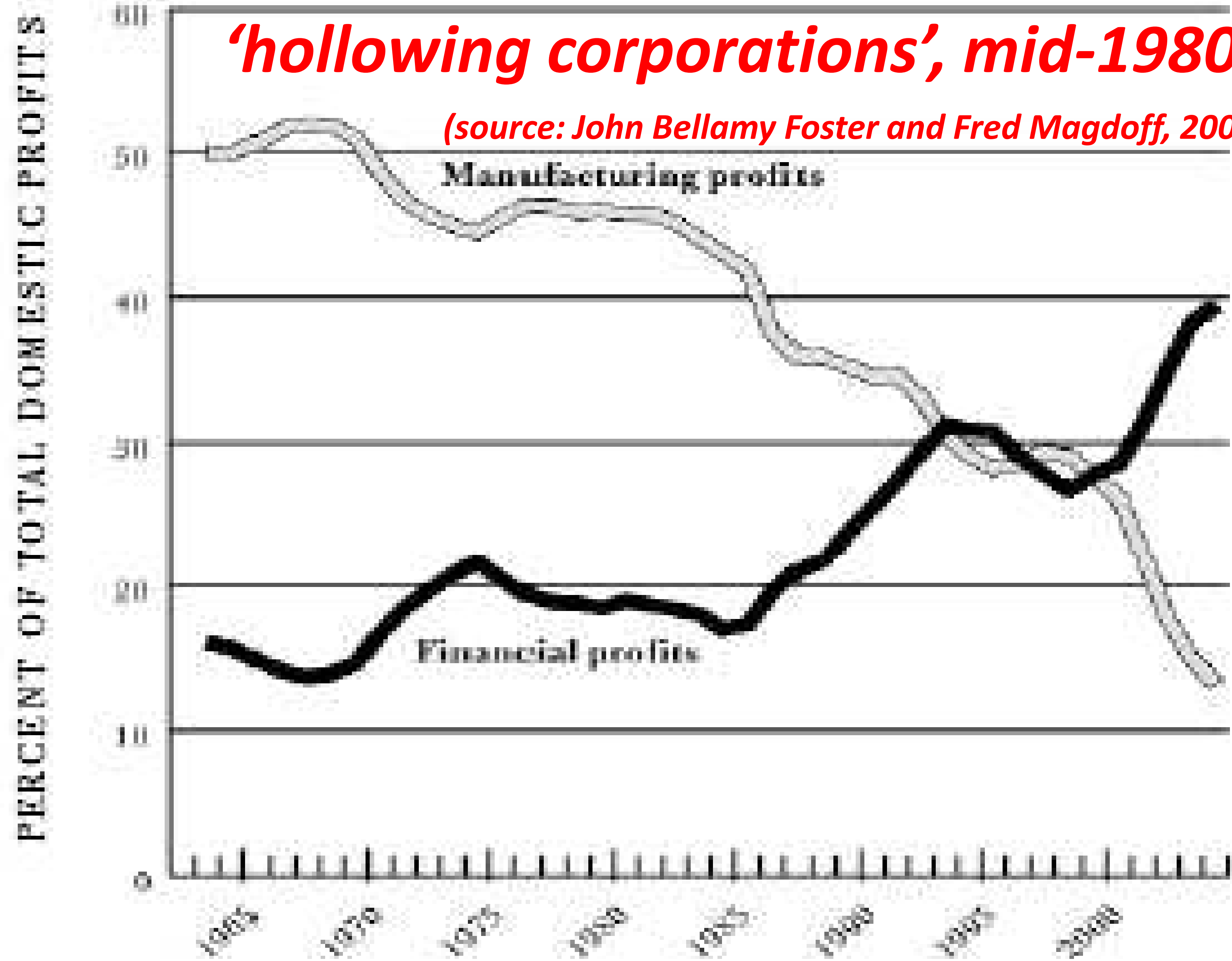
(source: John Bellamy Foster and Fred Magdoff, 2009)




US corporate profits become finance-addicted in mid-1980s
(source: John Bellamy Foster and Fred Magdoff, 2009)
FINANCIAL PROFITS AS A PERCENTAGE OF TOTAL DOMESTIC PROFITS
40
35
30
25
20
15
10
1965
1970
1975
1980
1985
1990
1995
2000
2005

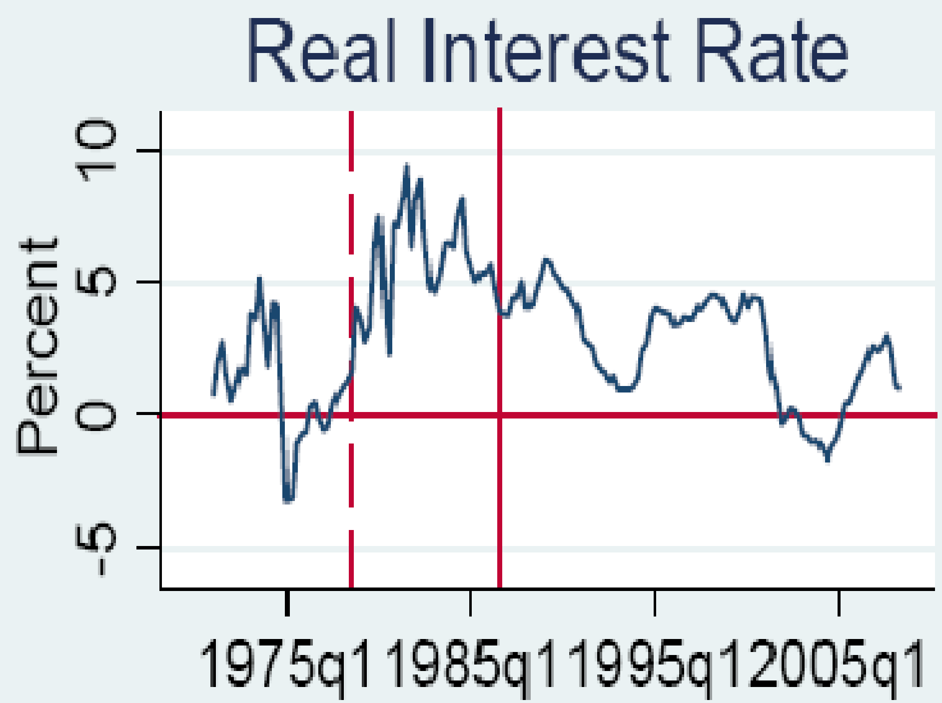
‘hollowing corporations’, mid-1980s

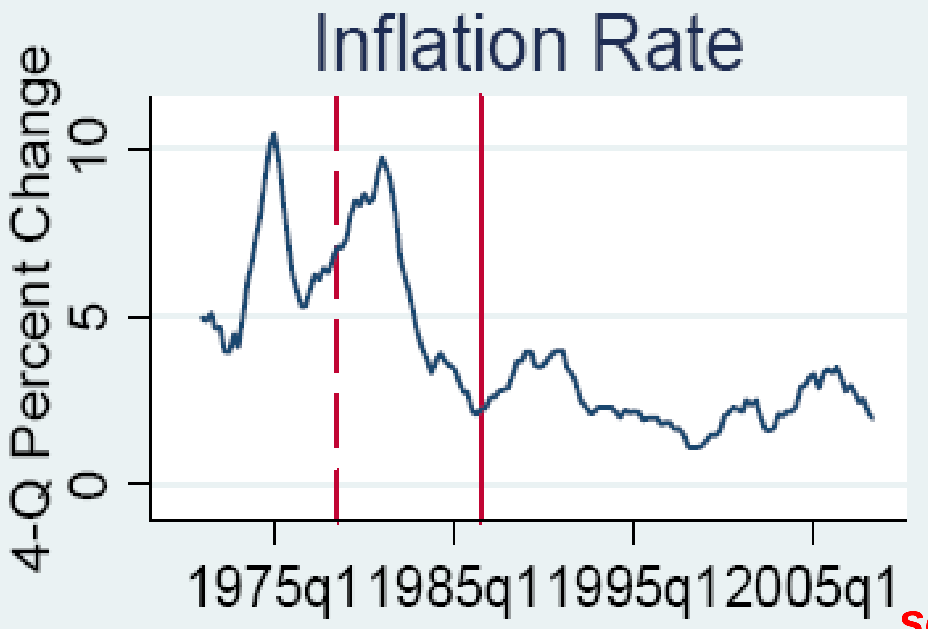
(source: John Bellamy Foster and Fred Magdoff, 2009)



How US economy fooled economists and investors for 20 years

- **Low interest rate**
- **Low inflation rate**
- **Low unemployment**

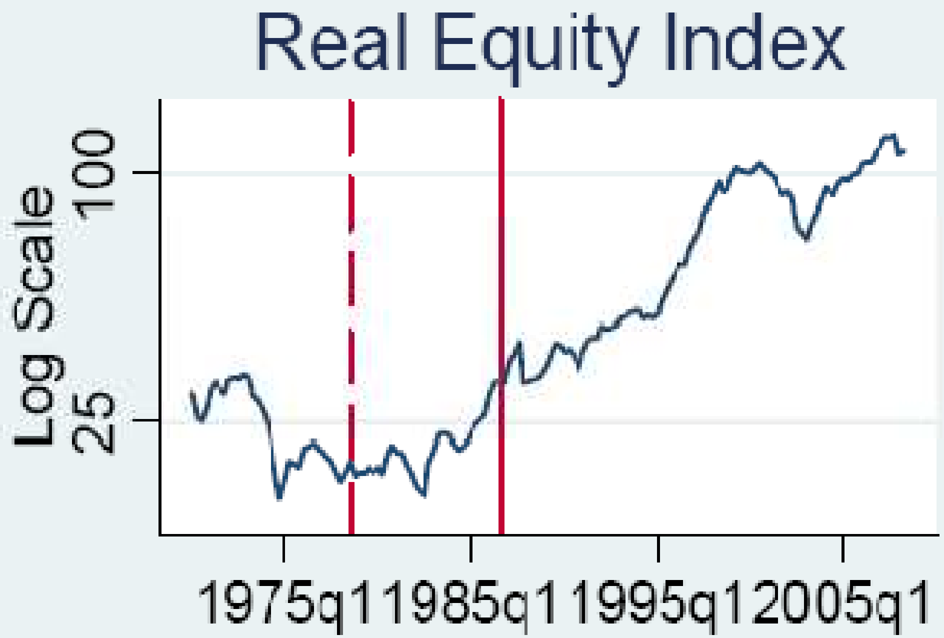


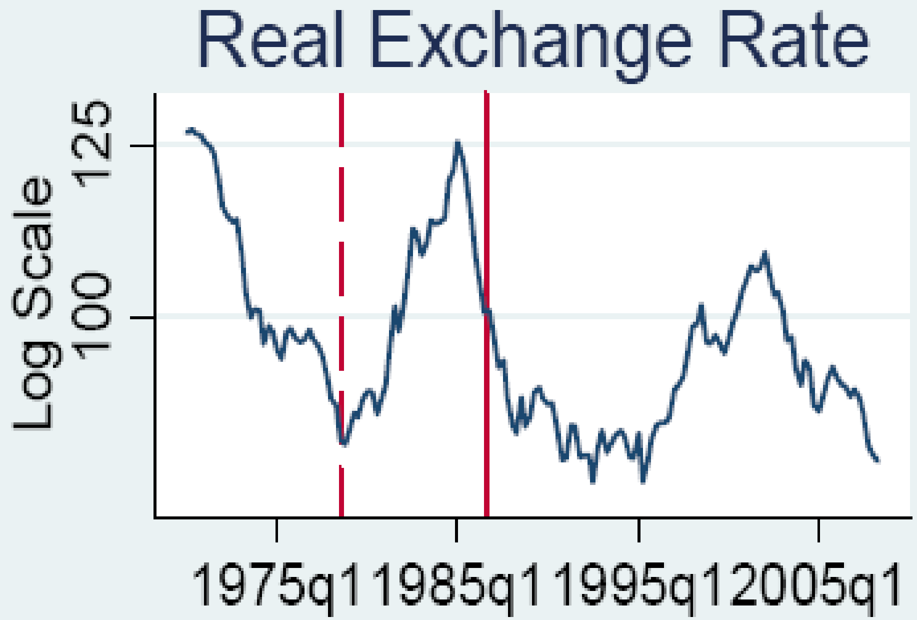


source: US Fed, Gagnon, 2009

How US economy fooled economists and investors for 20 years

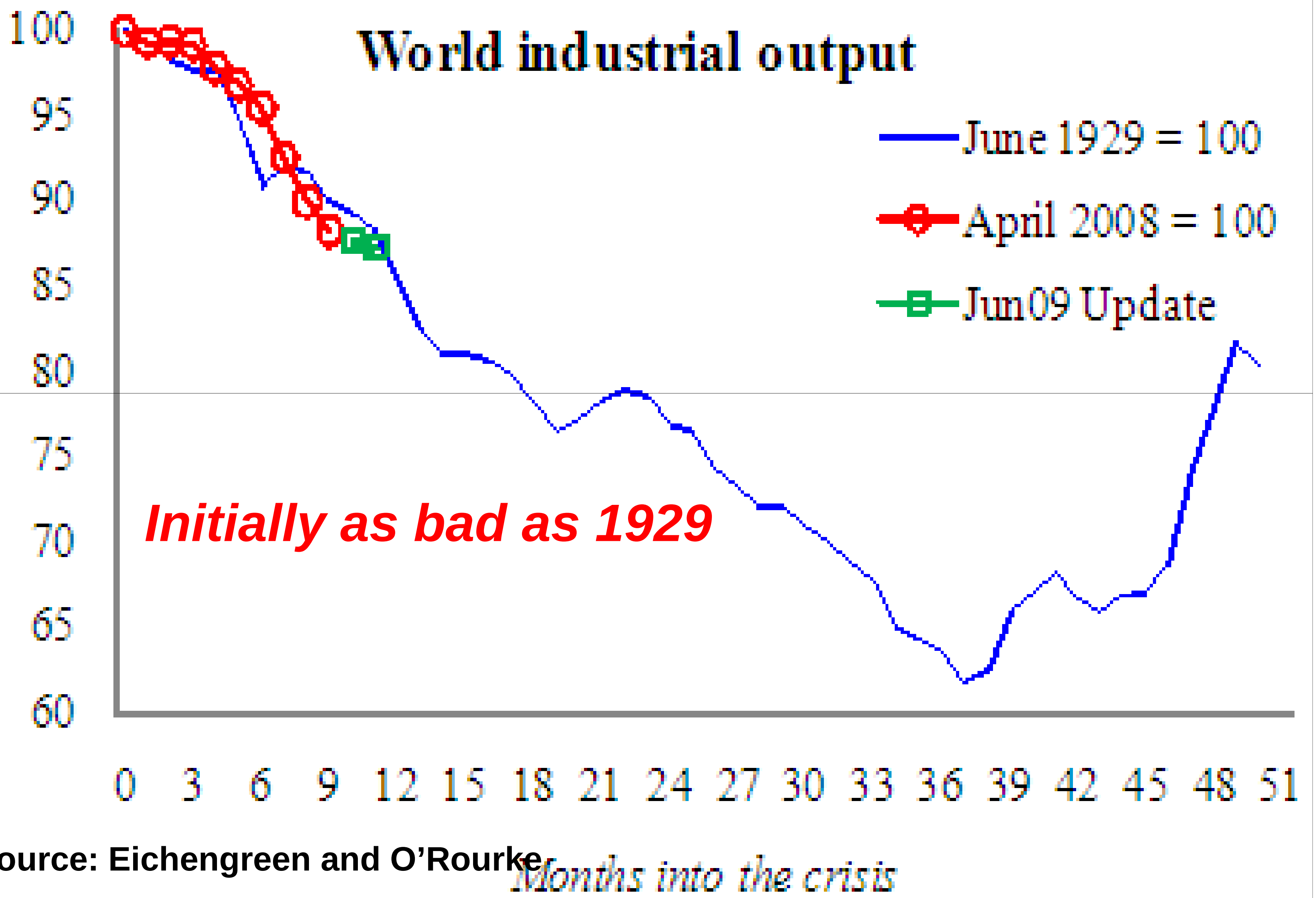
- steady GDP
- rising stock market
- recovery from currency volatility





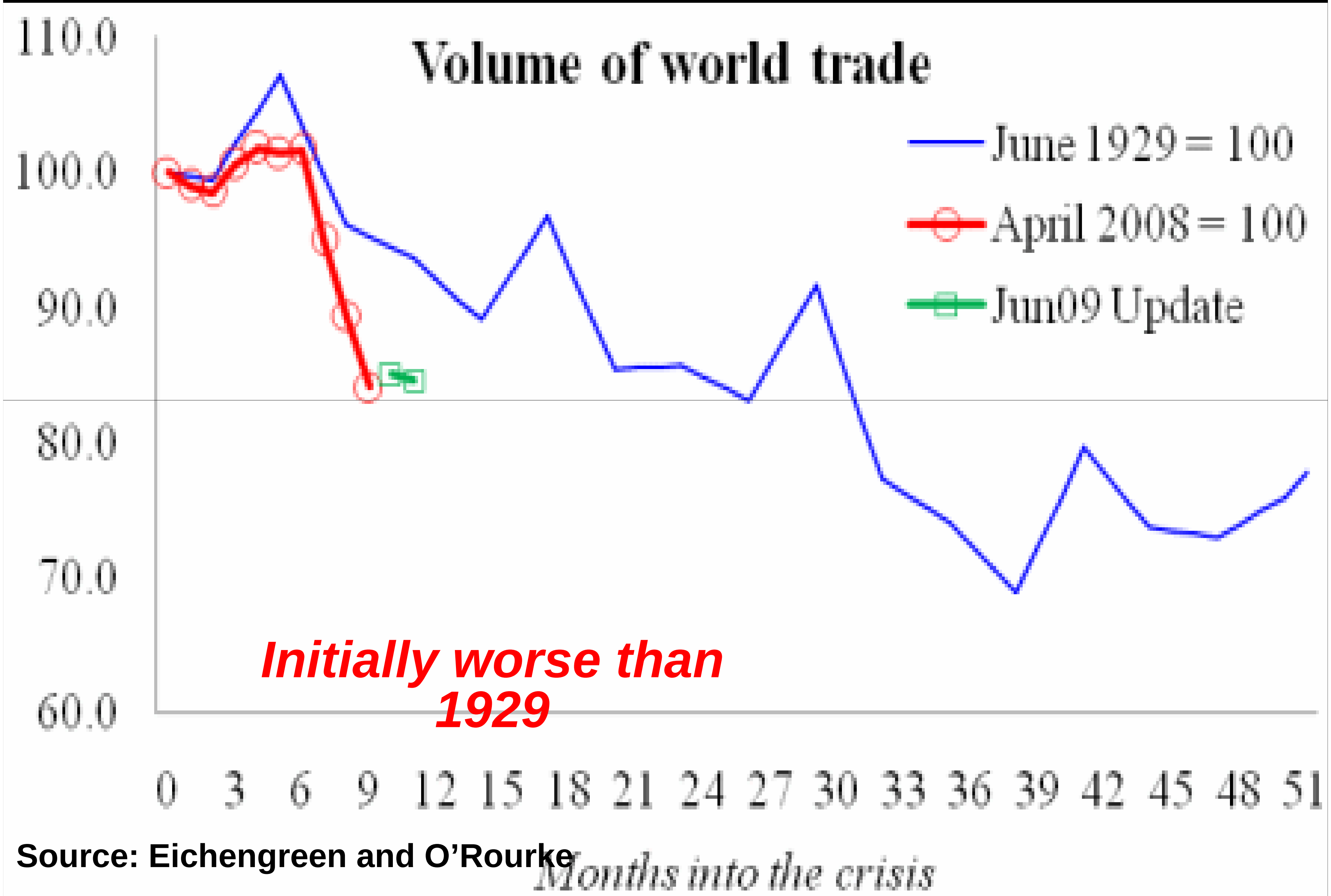
source: US Fed, Gagnon, 2009

Production crash in historical terms



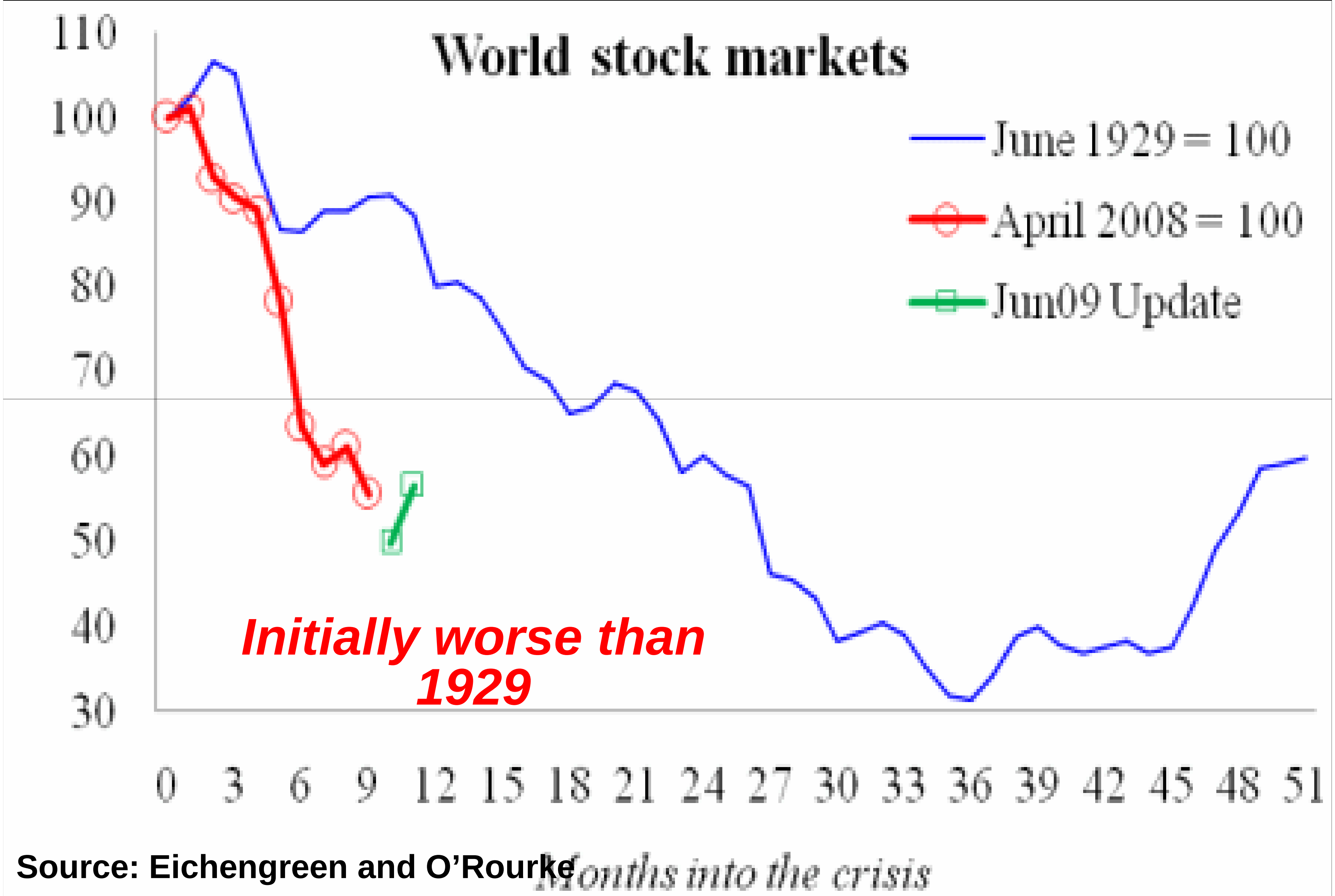
Source: Eichengreen and O'Rourke

Trade crash in historical terms



Source: Eichengreen and O'Rourke

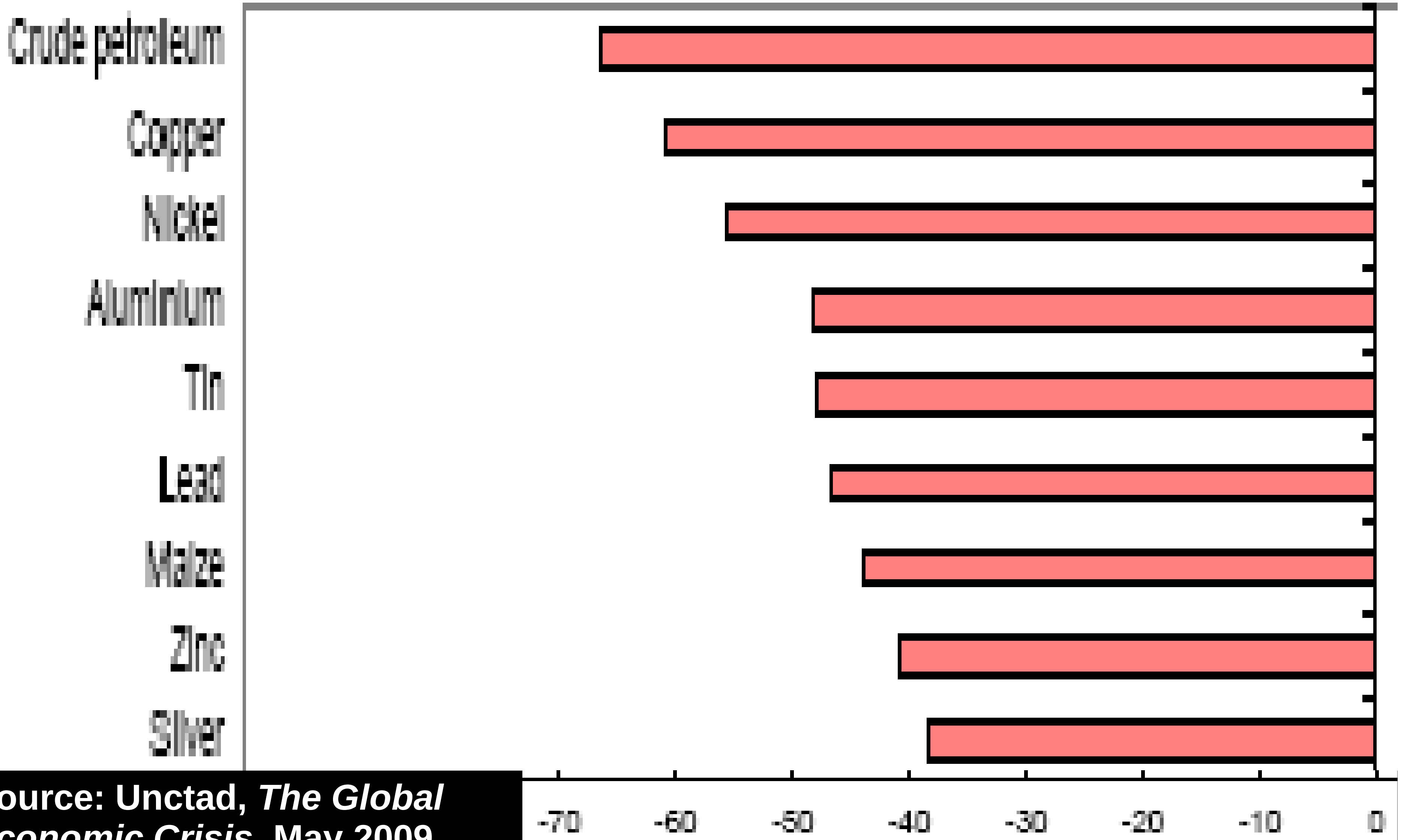
Stock market crash in historical terms



Source: Eichengreen and O'Rourke

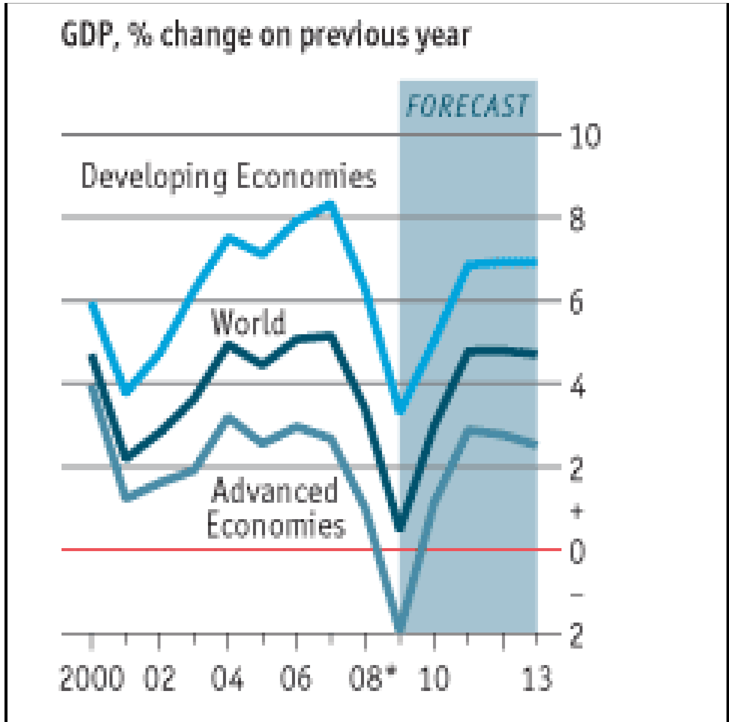
Commodity devaluations:

Change in prices, July – December 2008



Source: Unctad, *The Global Economic Crisis*, May 2009

Crash of GDP, industrial production and FDI

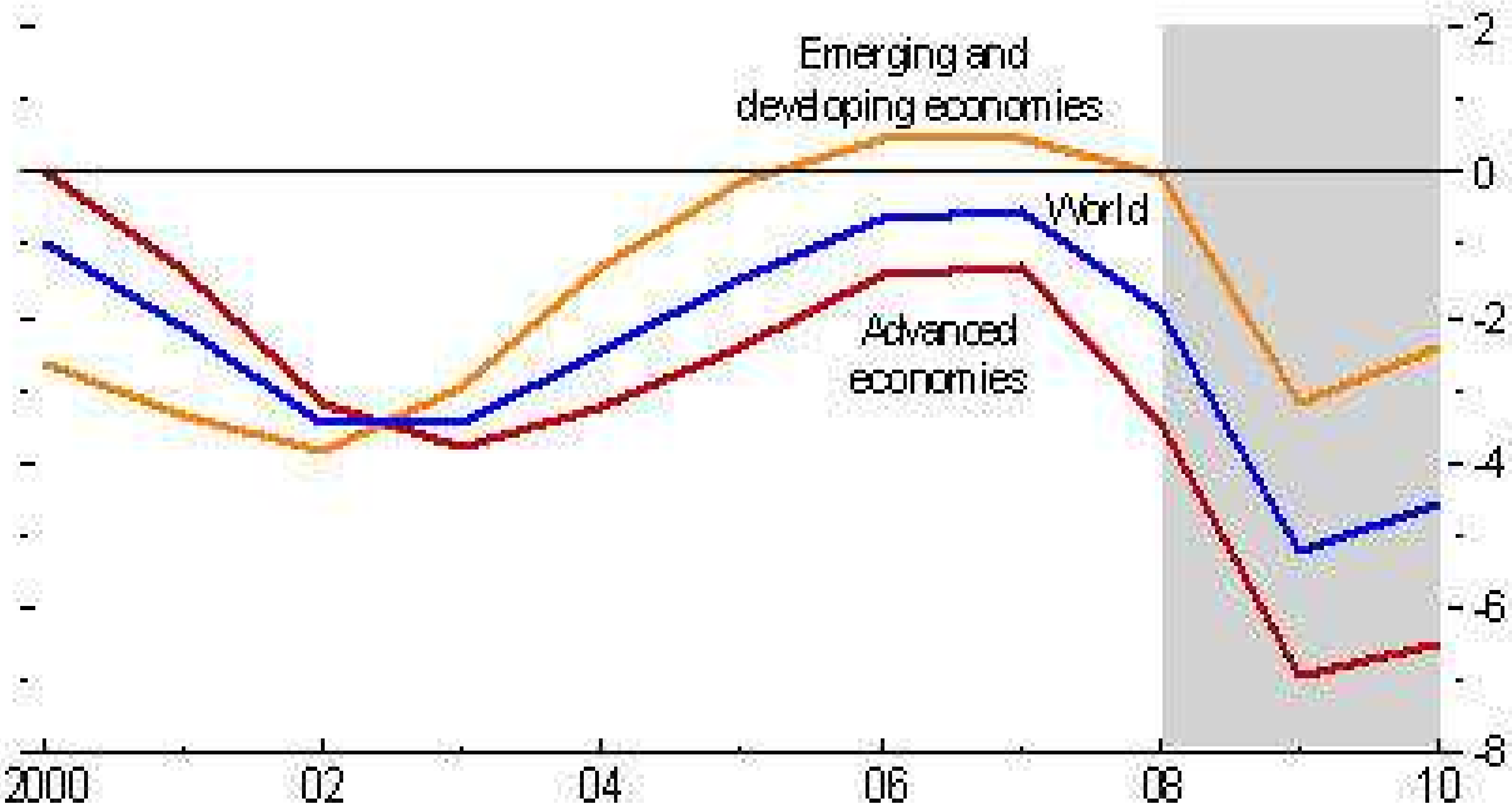


FDI inflows, % change on previous year
2008

Country	Change
Singapore	-57.3
Britain	-51.2
Germany	-48.9
France	-27.7
Japan	-22.7
US	-5.5
China	10.7
Russia	17.5

Source: The Economist

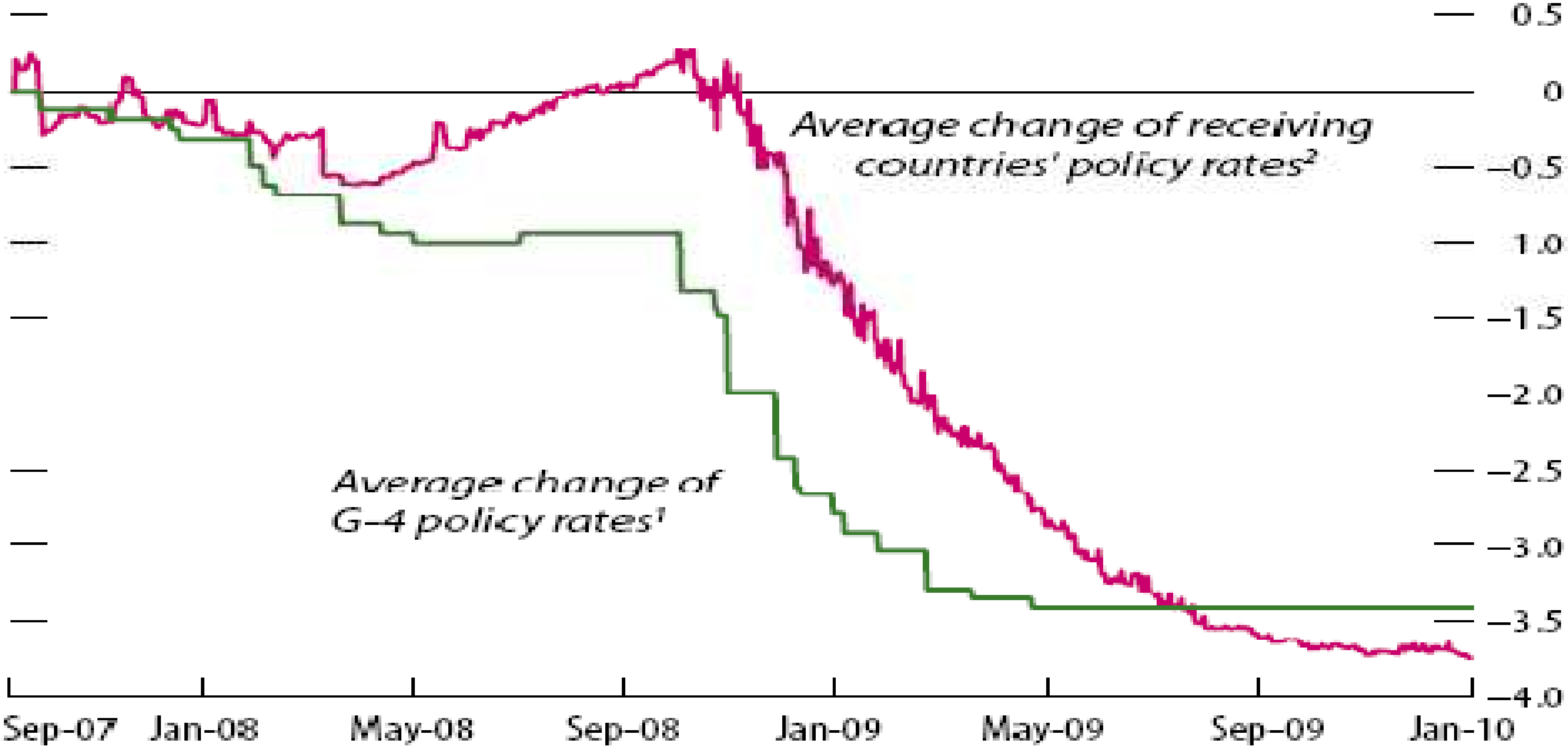
(Percent of GDP)



Source: IMF staff estimates.

Figure 4.2. Change of Central Bank Policy Rates

(In percentage points; September 1, 2007 – 0)



Sources: Bloomberg L.P.; and IMF staff estimates.

¹G-4 includes the euro area, Japan, the United Kingdom, and the United States.

²Receiving countries are Argentina, Australia, Brazil, Canada, China, India, Indonesia, Korea, Mexico, Norway, Russia, Saudi Arabia, South Africa, Sweden, Switzerland, and Turkey.

Source: IMF, *Global Financial Stability Report*, April 2010

Since the beginning of the financial market turmoil in August 2007, the Federal Reserve's balance sheet has grown in size and has changed in composition. Total assets of the Federal Reserve have increased significantly from $869 billion on August 8, 2007, to well over $2 trillion.

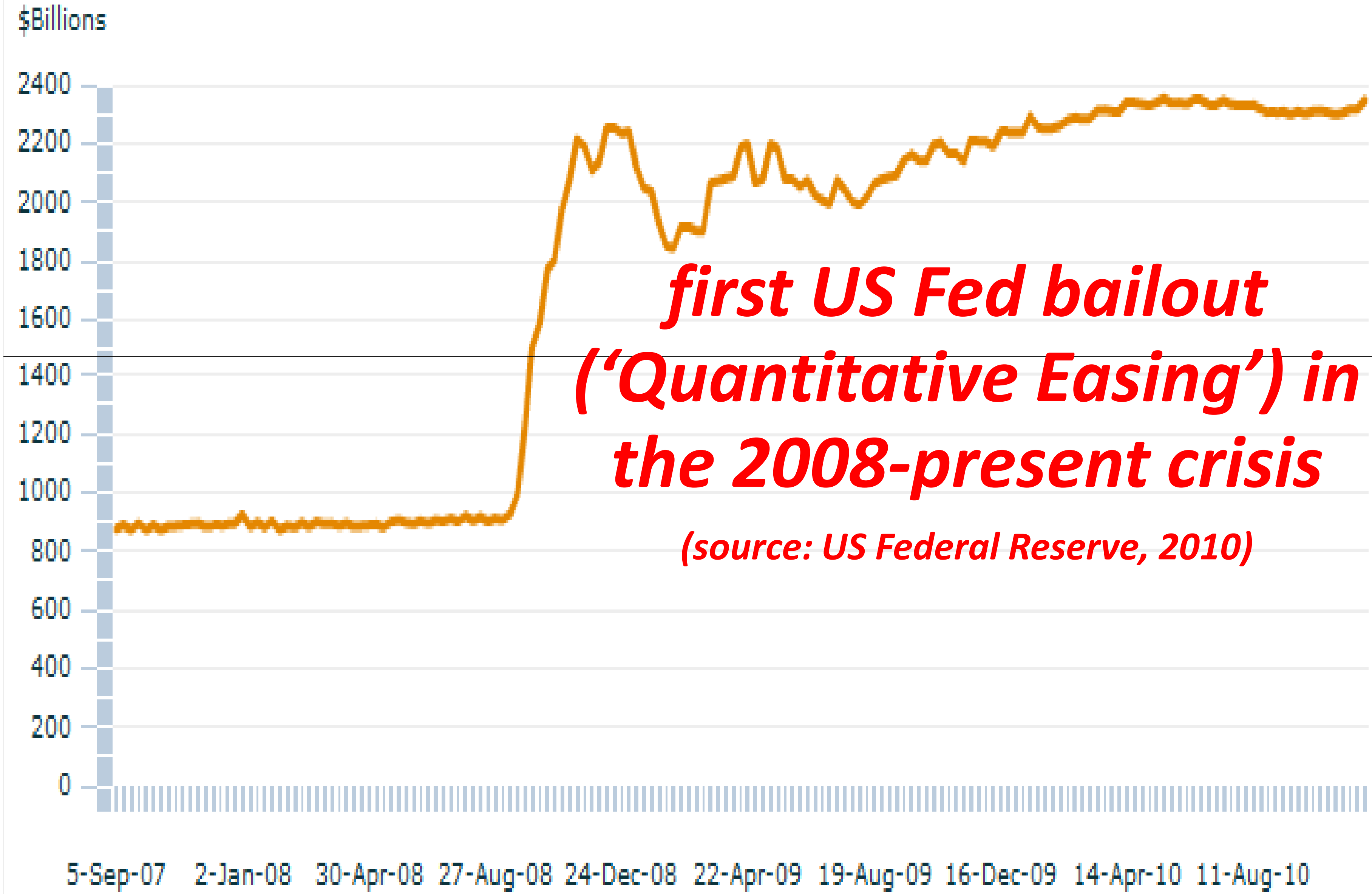


Figure 4.1. Global Liquidity

(In billions of U.S. dollars; GDP-weighted; quarterly data)

Source: IMF, *Global Financial Stability Report*, April 2010