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Globalisation, Crisis and the Political Economy of the International Monetary (Dis)Order

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ABSTRACT This article argues that the origins of the financial crisis of 2008 reside in the conditions of economic globalisation in the context of an imperfect world monetary order. It first describes the emergence of globalisation, after the demise of the Bretton Woods Monetary System, as a 'historical structure' in which financialisation has become the dominant mode of capital accumulation. It next outlines the interregnum period of a petrol-backed dollar reserve currency that underpinned, for a time, US hegemony. The concluding sections explore the consequences of the present crisis, the decline of the US dollar and alternative scenarios of world monetary order.

Este artículo sostiene que los orígenes de la crisis financiera de 2008 residen en las condiciones de la globalización económica dentro del contexto de un orden monetario imperfecto. Primero describe el surgimiento de la globalización, después de la extinción del Sistema Monetario Bretton Woods, como una ‘estructura histórica’, en la cual la financiación ha pasado a ser el método dominante de la acumulación de capital. Luego subraya el período interregno de una reserva de divisa respaldada por el petrodólar que sustentó, por un tiempo, la hegemonía de los E.E.U.U. Las secciones conclusivas exploran las consecuencias de la actual crisis, la decadencia del dólar estadounidense y los diferentes escenarios del orden monetario mundial.

本文认为，2008年金融危机的起因在于不完善的世界货币秩序下的经济全球化状况。它首先描述了在布雷顿森林货币体系瓦解后，全球化的出现作为一种“历史结构”而存在，在这种“历史结构”中，金融化已成为资本积累的主要方式。接着，本文概述了由石油支撑的美元储备货币（它一度加强了美国霸权）的权力空白期。结论部分探讨了当前危机的后果、美元的衰落和世界货币秩序的替代方案。

Keywords: globalisation, financial markets, global political economy, world currency, dollar hegemony
‘I believe that banking institutions are more dangerous to our liberties than standing armies. If the American people ever allow private banks to control the issue of their currency, first by inflation, then by deflation, the banks and corporations that will grow up around the banks will deprive the people of all property until their children wake-up homeless on the continent their fathers conquered’ (3rd US President Thomas Jefferson, 1802 cited in Tremblay, 2009).

There have been a wide variety of analyses of the financial crisis of 2008 and while many have sought explanations in the greed of individuals or the irrational behaviour of financial markets, it is only within the Marxist tradition that we encounter approaches which search for answers in the unfolding dialectics of capitalism as a system, with different strands prioritising different contradictions, stemming either from the declining rate of profit or the lack of realisation of surplus value due to overproduction or the concentration and centralisation of capital, or any one, two, or all three of these. Whichever of these causes one favours, the consensus seems to be that since the last major crisis in the 1970s, the world capitalist system temporarily overcame its contradictions by morphing into a new stage or mode namely, that of globalised financialisation. As a concept financialisation is not easy to pin down other than by saying that it has to do with money being made out of the circulation of money rather than by investment in production and trade. In the process, money is sucked out of the real economy and into the stratosphere of pure finance. We will return to this below.

But while there is thus a wide canvas of opinions I have also been struck by some similarities. These similarities are sins not of commission but of omission. And it is these that I want to address. First, although the growth and expansion of financial markets is widely seen to have started, together with globalisation, some time in the 1970s after the demise of the Bretton Woods System, there has been relatively little interest in pinpointing ‘globalisation’ itself as a cause of this ‘financialisation’. Second, there has been an over focus on the US sub prime mortgage market, and more widely the connected derivatives market. And while many, certainly on the left, have recognised that these are not causes of the crisis but mere symptoms of a deeper malaise, there has been comparatively little discussion on the political economy of the international monetary (dis)order, in particular the significance of currency markets, their volatility, size and ‘organised’ behaviour, and their role in the lead up to present crisis. The G20 in its communiqué after the Pittsburgh meeting on 25 September 2009 equally ignored the currency markets and stands firm on the benefits of globalisation.

Connecting these two, globalisation and the political economy of the international monetary (dis)order, my argument in this paper is that the financial crisis of 2008 is a crisis of globalisation in a world in which there is no one single monetary power. In a concluding section I explore the prospects for the dollar’s reserve currency status, its demise and its possible replacement by a new global currency.

Methodological Note: Historical Structure

In what follows the reader will stumble across a methodological conundrum: on the one hand I shall give a definition of globalisation which privileges the technological infrastructure of the information revolution, and which, in consequence, dates the onset of globalisation from the beginning of the 1980s. On the other, I also argue that the instabilities and volatility in the international monetary order which erupted after the breakdown of Bretton Woods in 1971 created the opportunities for, and sparked the beginnings of, the expansion of the international financial markets, and the invention of financial risk arbitrage instruments which—I claim—have
ultimately led to the financial crisis of today. In short, it begs the chicken and egg question: which came first—globalisation or financialisation?

Following Robert Cox I believe that in the study of social transformations we are less concerned with precise chronological sequencing than with the coherence of historical structures. Cox defined a ‘historical structure’ as a ‘particular configuration between ideas, institutions and material forces’. He argued that a relatively stable period of world order is one in which there is ‘a coherent conjunction’ (Cox, 1981, p. 135) between ideas (the prevalent image of world order including certain norms), institutions which administer the order with a certain semblance of universality, and material forces which include both material capabilities and the social forces engendered by the production process (Cox, 1981, p. 139). Abandoning historical materialism, both in respect of the supposed unidirectional connection between material base and superstructure in which material forces were always seen to change first, as well as in respect of its teleological determinism, he firmly retained the principle of the dialectic as the source of transformative change. The task of the critical social scientist is to study contradictions in social life as the mainspring of social change and to search for plausible alternative futures.

Looking through this methodological lens, I argue that with the collapse of the Bretton Woods monetary system, a relatively stable period of world order ended and was followed by crisis ridden years in the 1970s during which shoots of capitalist renewal emerged which included new international financial arrangements and practices. These could, however, only take firm root with the invention of new material capabilities in the shape of the information revolution in the 1980s. In time, they were also complemented by new institutional norms and practices (liberalisation, privatisation and deregulation), and a supporting legitimating, ideological framework (neo-liberalism). And thus a more or less coherent historical structure emerged. The fact that one particular feature of a complex configuration evolves as its dominant and defining characteristic, does not mean that it must appear first in the historical sequence of events.

**Globalisation and Financialisation**

Run of the mill definitions of globalisation typically refer to an increase of international trade in goods and services, the internationalisation of production and real investments; the increased integration of financial markets and a high degree of policy convergence among countries (WTO, 1998, p. 35; Sakbani, 2008, p. 3). All of these indeed belong to the complex ‘historical structure’ of globalisation but such definitions do not distinguish between the accumulation and the regulatory aspects of globalisation, and at best only describe aspects of it. But what is it fundamentally? What is at its core?

Following Manuel Castells (1996), and other sociologists (Harvey, 1989; Giddens, 1990) I would argue that globalisation is fundamentally connected to the ascendancy of real time over clock time, or time/space compression. The technological innovation which spurred this time/space compression was the fusion of telecommunications and information technology, usually referred to as ICT. This fusion can be timed precisely in the beginning of the 1980s. This information revolution broke down barriers between geographically dispersed markets, thereby giving rise to virtually instantaneous, electronic trading in financial markets. As we shall see further below, the information revolution also proved to be an important spur to the securitisation of markets (where debts are pooled together and sold on to third parties) because it reduced the need for a direct relationship between borrower and lender and the systematic treatment of large amounts of data on the creditworthiness of individual firms.
made it possible for more and geographically dispersed borrowers to enter the market (UNCTC, 1988, p. 106).

The ascendancy of real time over clock time meant that the core dichotomy between capital and labour was fundamentally altered with capital operating in real time and labour continuing in clock time. As Castells put it, capital hence could escape into the hyper space of pure circulation, while labour dissolved its collective entity into infinite variations of individual existences. In other words, it disappeared as a social force. Under conditions of the globalised informational economy capital became globally coordinated while labour became individualised (Castells, 1996, p. 476).

Within capital, furthermore, it is the financial sector in its pure monetary form that has moved along furthest in respect of ‘real-time’ (or if you like, electronic) transactions. The frenzied velocity of money flows on the foreign exchange markets alone averages about $3 trillion per day (cf. BIS, 2007, p. 1.), adding up on an annualised basis to roughly 20 times world gross domestic product (GDP). In their much acclaimed book, *Global Financial Regulation, A Handbook*, Howard Davies and David Green (2008, p. 4–5) report that the ratio of all financial assets to world GDP tripled from 109 in 1980 to 316 trillion in 2005.

The over-bloated financial sector has come to dominate and direct all other sectors, literally sucking the life blood out of them as profits made in the lower sectors of clock time commerce and investments are siphoned off into the hyperspace of pure circulation. I remember being very awed when it was first reported sometime in the late 1980s that first, the automaker Porsche, and subsequently nearly every other industrial corporation in some years, were making more money in the money markets than from producing cars or widgets or whatever. In 2006 some 40% of all corporate profits was accrued to the financial sector (Summers cited in Gowan, 2009).

In respect of the trend towards the extraction of surplus from the ‘real economy’ to the financial hyperspace of pure circulation, Charles Morris (2008, p. 151) gives these startling figures relating to the US economy: ‘from 1980 through 2007, total employee compensation, including benefits, dropped from 60.1% of GDP to 56.3%; the ratio of investment to corporate profits was halved; and the share of GDP going to cash dividends nearly tripled’.

The trend figures of income inequality in the US reinforces this picture: between 1980 and 2006 the top tenth of the population’s share of all taxable income went from 35% to 49%, an increase of about a third. But almost all the top tenth share gains themselves went to the top 1% who more than doubled their share of national cash income from 9% to 20% (Morris, 2008, p. 152). As there is only so much even the wealthiest, greediest, and debauched of men can spend on consumption, most of this increase in income inevitably flowed back into financial assets, thus increasing once again the money supply available in financial markets, ultimately destabilising these markets as increasingly shaky and risky financial instruments (like sub prime mortgage Collateralized Debt Obligations (CDOs)) were having to be invented to soak up this liquidity.

Thus, as Castells presciently forewarned in 1996, the annihilation and manipulation of time by electronically managed global capital markets are the source of new forms of devastating economic crises (Castells, 1996, pp. 436–437).

**Financial Markets, Boom and Bust**

How did we get to this point where money careens around the world in an over-bloated frenzy of money creation?

In a most entertaining book on the history of financial speculation, *The Devil Takes the Hindmost*, Edward Chancellor (2000) describes how almost every transaction, however speculative,
and sometimes corrupt and fraudulent, that we witness today in the financial markets was known
from the days that the stock markets first emerged in seventeenth-century Amsterdam. These
practices included derivatives and even futures contracts.

Chancellor takes us through the history of all the booms and busts that have blotted the land-
scape of capitalist progress through the centuries. From the Tulip Fever in Amsterdam in the
mid-1630s, and the South Sea Bubble in London in the 1720s, through the first Latin American
debt crisis (1820s), through all the manias of the nineteenth century, the canal mania, the railway
mania, the mining mania, on to the crash of 1929, and beyond, to the stock market crashes of the
late twentieth century. What is striking, as Chancellor never tires of pointing out, are the obvious
similarities in these boom and bust cycles despite the minor differences which are historically
specific. And he quotes Kindleberger: ‘details proliferate, structure abides’ (Kindleberger in
Chancellor, 2000, p. 53). Periods of speculative mania are forever followed by anti-speculative
regulation when governments wake up and rein in whichever financial fad or gimmick is seen to
have caused the excesses.

And so, if history just repeats itself, the question arises, why should this crisis be different?
Different, not merely as in order of magnitude, because it is global, but different as in systemic?
Systemic in a way that cannot be put right by government regulation, even if—and it is a big if—
inter-government cooperation such as is earnestly being attempted in present day world econ-
omic summits, succeeds in the limited objectives of oversight and coordination that are
formulated?

The answer I suggest has to do with the circumstance that financial globalisation and the arbi-
traging of risk today takes place in markets where there is no longer a single monetary power.

The Political Geography of Risk

One hardy perennial in mainstream narratives of capitalist crises is a stubborn refusal to take
account of the political arena in which these crises occur. The economic sphere is forever
depicted as some independent realm in which individuals go about their rational self-seeking
business without much interference by political authorities or collective concern for political
goals. For sure there is often plenty of critique and condemnation of individual instances of
corruption, and of manipulation and venality by members of the political class, but rarely
does one find a conception of the way the economic arena is importantly structured by political
interests of classes or groups of people, and in the international arena by power relations
between states.

Even if one were to argue that in the past, at least, most financial and commercial transactions
occurred within the national territorial context (although this too is arguable, see below) it is still
surprising that in the contemporary era when clearly by far the fastest growing markets are the
international currency markets, the political terrain of currency competition between states is
largely ignored. And yet, the right to print currency, and set interest rates, is probably the last
remaining seigniorial right of the sovereign state. Amending Castells’ important dictum that
in the era of globalisation, the power of flows overtakes the flows of power I would argue
that today, the international currency markets are the terrain where the power of flows do not
overtake but collide with the flows of power (Castells, 1996, p. 476).

Let us look a bit closer at the origin of the international credit and currency markets.

International credit flows, in the form of international direct investments and portfolio lending
(bank lending, and bond issuance) have a existed for a long time. The period of formal coloni-
alism, especially between 1875 and 1914, witnessed an extraordinary and globe-girding
internationalisation of capital when a handful of countries in Europe together with the USA were responsible for 85% of all international lending totalling, by 1913, $44 billion. As the distinguished economic historian Alex Cairncross (1975, p. 3) observed, ‘It was symptomatic of the period, that western Europe had invested abroad almost as much as the entire national wealth of Great Britain, the leading industrial country, and a good deal more than the value of the capital physically located in Great Britain’.

Now credit, of course, as the root of the word reminds us, means *credo*, or faith. Where did the faith and confidence for these far flung international transactions come from? In no small measure it came from the political power and force that accompanied it. That was what the gunboat diplomacy of the early pre-colonial period (the Dutch East India trading company VOC had a private army of 10,000 men), and next the territorial annexations of the colonial period, was all about. It was about establishing world wide economic and financial relations by force. Moreover, during the colonial period, the mother countries established ‘monetary zones’ (the sterling area, the franc zone) in their dependencies where the value of the currency was linked to the mother currency and colonial reserves were kept in the mother country’s central bank. There was not much need, therefore, for hedging against either commercial or currency risk.

After the end of World War II, when the US and its allies emerged victorious, the colonial system was dismantled, while on the eve of the end of the war, the international conference at Bretton Woods in 1944 had established a monetary order to fix exchange rates. It is a well known story. The two intellectuals who drafted the settlement, the British John Maynard Keynes, and the American Harry Dexter White, agreed on many things but diverged on some crucial issues: where Keynes wanted a world currency, the Bancor, against which all national currencies would be exchangeable at fixed rates, and an International Clearing Union, a kind world central bank, White proposed the use of the dollar—at fixed parity against gold—and the International Monetary Fund as a stabilisation fund. The American view held sway. For a while, under the aegis of this American imperial system international trade and investments proceeded, indeed expanded, relatively smoothly. But over time this historical settlement was brought down by its own contradictions. The de facto ‘dollar standard’ led, over time, to an overvaluation of the dollar, and a massive outflow of American capital. The consequent prolonged US balance of payments deficit thus became a principal source of international liquidity and gave rise to ‘offshore’ or ‘eurodollar’ markets. The practical impossibility of reverting these offshore dollars into ‘native’ dollars, due to the restrictions of the Bretton Woods agreement which precluded a reassessment of the value of the dollar, and political/diplomatic pressures by the US government on the central banks of Europe, led to speculative movements against the dollar in these markets. By 1971 these speculative movements had reached such crisis proportions that in August 1971 the US government, under Nixon, declared the dollar no longer convertible into gold, thereby effectively ending the Bretton Woods exchange regime. A 10% devaluation of the dollar soon followed.

The consequences of this were two fold: on the one hand a tremendous increase in volatility in the international currency markets and on the other, more generally, a huge increase in international credit risk. Companies or banks investing abroad would have to run the whole gauntlet of volatile currencies as well as the commercial risk of dealing with counter parties who could go bust or default in countries where there might not be effective legal redress possible. This increase of risk, over time, led to the invention of a whole class of new financial instruments, to spread risk, to reduce exposure and to insure against risk; the most important of these being, besides futures and options, currency swaps, interest rate swaps, Credit Default Swap
(CDS), and the CDOs. What began as earnest ‘hedging’ against risk soon developed into a source of endless speculation and gambling.4

First came the currency swaps and currency futures (the first currency futures market was opened in 1972, in Chicago) and later on, from the 1980s when policies of liberalisation and deregulation of financial markets had become established world wide, there developed a huge wizardry of new financial derivatives. A financial derivative is a security created by contract, which derive its value from some underlying asset. For example, you take out a futures contract on a commodity, like oil, and the contract says you promise to take delivery of this oil at a certain date for a certain price. If the price is higher than what you bid for it you win, if it is lower you lose. Since you only have to make a down payment of say about 5% at the time of the contract, you just gamble on being lucky (and in the process become part of the credit creating process). In the past there was a legal distinction between pure gambling (in which there is always settlement in cash) and derivatives where you were supposed to always take delivery in the specified commodity, but part of the ‘deregulation’ of financial markets was that this legal distinction was abandoned.5

A subsequent development was securitisation. Securitisation simply means loan selling. It is really about turning debts into assets and selling the fixed income (interest payments flowing from them) on to third parties. The elegant idea behind it is that by pooling debts such as mortgages or car loans and credit card loans and company start up loans into bonds and parcelling them out in little chunks you can de-link borrowers from lenders and spread the risk of all these debts over a wide political geography. And you can offset the poor risks under the better performing loans (for an early discussion on this, see Hoogvelt, 1997, p. 82). This is the origin of the much decried CDOs.6 They became really big in the 1990s and at the height of the sub prime mortgage disaster, the size of the CDO global market is estimated anywhere between $500 billion and $2 trillion.

The Political Economy of the Currency Markets

Now let us bring the power of states into this soup of global credit flows. Hard on the heels of the end of the Bretton Woods era came the oil shock of 1973 when the OPEC countries formed a successful cartel of oil producing countries and increased the price of oil four fold. Now why did they do this at exactly that time? Mainstream economic discourse, which habitually underplays the political context, cannot offer a satisfactory explanation. But documentary evidence uncovered by writers standing in the critical Marxist tradition who are more attuned to the interplay between politics and economics have come up with an altogether plausible version of events that places the blame not at OPEC’s door but on the Nixon administration, which was desperate to regain control over the global money markets and safeguard the interests of American capital (cf. Fitt et al., 1979; Gowan, 1999; Engdahl, 2004).

By the time of the Bretton Woods collapse, there were many more dollars circulating outside the USA than in. To prevent these dollars coming back in and causing intolerable inflation inside the US something had to be done about this ‘dollar overhang’ as it was called. The solution was to give these foreign dollars something to do that would create demand for them and force all states to keep the dollar as a reserve currency even in the absence of the now defunct Bretton
Woods monetary system. The Nixon administration was planning to get OPEC to greatly increase its oil prices a full two years before OPEC did so, and for the US private banks to recycle the petrodollars when OPEC finally did take US advice and jack up oil prices (Gowan 1999, p. 21; Iseri, 2009, p. 137). The scheme was ingeniously devised by Henry Kissinger, then Secretary of State and a good friend of the Shah of Iran (the Chairman of OPEC at the time). Kissinger’s scheme would kill not one or two but three, or even four, birds with one stone. First, it would solve the dollar overhang because oil transactions had always been settled in dollars and a deal signed in 1974 when Kissinger established the US–Saudi Joint Commission on European Cooperation, ensured that not only they would do so in the future, but that any surplus of oil price increases would be invested in US treasury bonds, stocks and mutual/hedge funds (Fouskas & Gokay, 2005). Second, it would deal a hopefully fatal blow to the challenges posed to US imperialism by the European states and Japan who were a serious competitive challenge but who were much more dependent on imported oil than the US was at the time. Third, it would give the OPEC countries the necessary surplus dollars to endlessly buy US military equipment (which they duly did—the Yom Kippur war in 1973 providing a convenient excuse). And finally it would help the—at that time—dominant US oil companies who needed an instant increase in revenues. So this was a brilliantly clever scheme and there is enough evidence today to suggest that this is exactly what happened. William Engdahl (2008a) reports that corroboration for this thesis was provided a few years ago in an interview with no one less than Sheikh Yamani, oil minister of Saudi Arabia at that time. ‘King Faisal sent me to the Shah of Iran who said: “Why are you against the increase in the price of oil? That is what they want? Ask Henry Kissinger – he is the one who wants a higher price”

So out of the demise of the Bretton Woods system came a US strategy for regaining reserve status for the dollar and US hegemony in the world monetary order. As Gowan (1999, p. 21) put it succinctly: the US administration understood the way in which the US state could use expanding private financial markets (post Bretton Woods) ‘as a political multiplier of the impact of US Treasury moves with the dollar’. This is how, what he calls ‘the Dollar—Wall Street Regime’ was born. Globalisation and the freeing of international financial markets from ‘financial repression’, as the Nixon administration referred to it, became key to preserving the privileged global position of the US. The change was summed up by Helleiner (in Gowan, 1999, p. 23) as a shift from direct power over other states to a more market based or ‘structural’ form of power. The Asian financial crisis of 1998 is, I believe, a good example of how this Dollar–Wall Street Regime used to work.

**Hedge Funds: Instruments of Financial Warfare?**

Hedge funds are private wealth funds that invest not in stocks or bonds directly but mainly in financial derivatives of all kinds, like currency futures and interest rate swaps and credit default swaps.

Even if one generously and innocently surmises that when hedge funds first appeared on the scene during the volatile currency heydays of the 1970s they provided a useful function in arbitraging risks in the currency markets, their subsequent exponential growth soon transformed them into becoming betting syndicates for the super rich.

The amounts of money they handle are mind bogglingly large because with the monies at their disposal they can leverage ever more monies in from banks and other financial institutions for their speculative activities. In the mid 1990s a study by the IMF (Vrolijk, 1997) estimated that hedge funds in the foreign exchange derivatives market could mobilise up to $1 trillion
to bet against currencies in speculative attacks. That is sufficient to wreck the currencies, the financial markets and the economies of most countries, as was the case during the Asian crisis of 1997–1998. Today there are about 10,000 hedge funds around the world with assets under management (AUM) amounting to $2.5 trillion (Chan, 2007). Hedge funds trade in risk, and they are completely unregulated, partly because regulators like the UK Financial Services Authority and the US Securities and Exchange Commission (SEC) by their own admission do not understand them, and partly because the regulators have, for political reasons, decided to collude with the wild frontiers of modern-day finance (Bush, 2006; Engdahl 2008a). To argue that hedge funds may be used and have been in the recent past (for example, during the Asia crisis of 1998) as instruments of statecraft begs three important questions, namely those of collusion, political coordination and intentionality.

The official neo-liberal consensus has always been that no one speculator can engineer structural shifts in prices on financial markets because there are so many players and they all act rationally in their own interest playing against each other in a zero-sum game. This for a start ignores the contagion effect or ‘momentum’ trading as it is now called as when one large speculator could, for example, off load the yen, which prompts other smaller participants to follow suit driving the price of the yen even further down, allowing the first to withdraw from his position, taking a profit. But, more importantly, it ignores the concentration of financial firepower within the hedge fund community. According to an IMF study in 1997 just 10 hedge funds at that time handled 75% of the business in the financial centres of the US, the UK and Canada (where nearly all world wide hedge fund activity takes place anyway). And these 10 worked very closely together and were dominated by the US funds (Vrolijk, 1997). Given the evident cross-staffing and the shared social milieu of the top political and economic elites (the outgoing US Treasury secretary Hank Paulson was one time Chief Executive of Goldman Sachs) it beggars belief that the highest and mightiest would not discuss common political/economic interests. At a charitable minimum, and to avoid the charge of conspiracy theory, one might say that they would have what is sometimes called ‘group think’ or ‘pensee unique’ as the French call it.

But what exactly are these common interests? In the aftermath of the Asian crisis of 1997 one could surmise that the Clinton administration had felt threatened by the competitive challenge of the East Asian emerging economies and was sufficiently irked by the financial regulations in place in these countries to want to unleash the destructive power of the hedge funds, and next engineer a rescue package duly implemented by the IMF that attached a structural reform agenda opening previously closed financial and economic sectors to international capital (Gowan, 1999, ch. 6; Gills, 2000; Krugman, 1999, pp. 133 ff; Hoogvelt, 2001, pp. 232 ff). And so it came to pass. Whether there was strategic planning on the part of the Clinton administration prior to the crisis, or merely a strategic handling of the crisis in the interest of deepening and furthering American dominated globalisation is not really what matters. What matters is that the fall of East Asia was both opportunistically and strategically seized upon by the USA to recoup the economic high ground, and that an alternative scenario involving a proposed Japanesed Asian Monetary Fund was scuppered, because the US relied on Japan’s and other East Asian dollar holdings which might have been sold to finance such a fund. Scuppered, too, was the consolidation of regional integration that such a fund would have implied (cf. Hoogvelt, 2001, pp. 236–237).

The question for the immediate future is whether the US administration can or will play the same strategic financial game in relation to China, whose currency and financial markets have been relatively shielded from the fall out of the global financial collapse thanks to the Chinese government’s control over its currency and capital markets. Can an imperialist...
collaboration between hedge funds and the US government succeed once more? Can the US
today still use private financial markets as a ‘political multiplier of US treasury moves with
the dollar’ as Gowan (1999, p. 23) put it? In short, does the United States still have ‘structural
power’? In the next sections I explore both internal and external limits to this structural power.

From Reserve Currency to Funding Currency: The Dollar Carry Trade

Future economic historians no doubt will argue over the exact date when, and the precise actions
whereby, the US administration finally and definitively lost control over the financial markets,
including its ability to determine the value of the dollar. In 1998 Clinton was famously defeated
by the international bond markets when he attempted to increase the US budget deficit and was
forced to abandon the strategy and instead balance the budget.

The Federal Reserve, established by the Federal Reserve Act of 1913, is a quasi-public banking
system, comprising 12 regional privately-owned Federal Reserve banks, numerous private US
member banks, as well as a presidentially appointed Board of Governors that acts as a government
agency. Unlike other central banks around the world it does not actually create the currency,
which is the preserve of the US Treasury, but it controls the money supply by setting interest
rates and conducting so-called ‘open market operations’, that is buying and selling government
bonds to the banking sector. The history of the Fed is littered with damning critiques and conspi-
racy theories to the effect that far from wresting democratic control over money from Wall Street,
it actually gave it back to the ‘money trust’ in spades (cf. Paul, 2009). President Woodrow Wilson
who secured the passage of the Act, is thought to have regretted his actions.8

The post crash 2008 policies by the US administration to bail out the banks and other financial
institutions deemed ‘too big to fail’ may well prove to be the final nail in the dollar coffin. In a
spirited but all too brief report Tremblay describes the various facilities and programs through
which the Fed and the US Treasury have channelled cheap funds to the banks and brokers. They,
in turn, have used these ‘near free’ funds, with leverage, ‘through their hedge fund like activities,
to buy interest-paying assets in the U.S or abroad’ (Tremblay, 2009). The upshot has been, apart
from a rise in stock markets, a rather new phenomenon, the ‘dollar carry trade’.9

The ‘carry trade’ is simply a code name for the strategy of borrowing (or buying) low-yielding
currencies in order to finance the purchase of riskier higher-yielding assets. In the years leading
up to the crisis, it was the Japanese yen that was mainly used for this highly market distorting
trade. Today the dollar is being used as a funding source for this trade. But whereas the yen
is not—and never was—a reserve currency, the dollar is. The whole point about a reserve cur-
rency is that it is meant to provide some stability to international financial transactions. With this
new function, it has become instead a source of instability and volatility in the financial markets
and this will encourage both governments and private markets to dump the dollar. On its own the
debauching of the dollar by the Obama administration may not be quite enough to undermine the
dollar’s privileged position as a reserve currency. But coupled with other, geopolitical, motiv-
ations it may well herald a profound shift in the hegemonic control of the world economy.

The Dialectic Legacy of the Asian Crisis

The Asian crisis of 1997–1998 left the Asian governments, including the Chinese government,
with no other option than to accumulate dollar reserves as a means of forestalling any future
attempts at hot money skullduggery (cf. Morris, 2008, p. 92). It was a sensible response, but
in the context of growing trade imbalances between the US and the rest of the world, it also
had the perverse effect of financing the US balance of trade deficit, thereby delaying the costs of real adjustment to the US dollar, cheapening credit in the US, and fuelling its housing and consumer booms.\textsuperscript{10} It also shifted most or all of the counterpart appreciations onto the euro and other freely floating currencies (Bergsten, 2008). Between 2002 and 2007 the dollar lost between 25\% and 50\% of its value against the main floating currencies, including the euro.\textsuperscript{11} At the same time the stand-off between the US and its Asian creditors significantly added to the volatility in the currency markets, increasing the volume of transactions in traditional foreign exchange instruments by 71\% in 2007 alone (BIS, 2007), and occasioning a spectacular rise in the Yen ‘carry trade’.

Because the Chinese pursued a dollar peg the renminbi could not rise against the dollar despite the flood of investment and speculative dollars coming in. To keep its fixed parity with the dollar the People’s Bank of China would buy foreign currency in exchange for the renminbi and withdraw all that extra domestic cash through issuing notes and bonds (a policy dubbed ‘sterilisation’). The ‘Chinese dollars’, in turn, were invested mostly in US treasury bonds and bills. The Chinese government’s action was widely condemned, especially in the US, as ‘currency manipulation’, and in the years leading up to the crisis it led to considerable pressure on China to unpeg and revalue its currency which it finally did in 2005, although in a fashion more symbolic and limited than effective, and far from sufficient to silence the critics.

A Global Currency?

Both in the run up and in the wake of the crash of 2008 there has been a crescendo of voices advocating various pathways toward a new monetary order with either a single global currency, or—as a first step—a global unit of account, acting as a replacement for the dollar as reserve currency, concurrent with moves toward a global system of governance or a kind of world central bank. Distinguished academics like Joseph Stiglitz, Robert Mundell, and James Tobin have taken up the cause of a single world currency (cf. Marshall, 2009). The BRIC nations (Brazil, Russia, India, and China) at their June 2009 summit in Yekaterinburg, Russia, called for a new global reserve currency, following earlier demands by the Chairman of the People’s Bank of China, Zhou Xiaochuan, for a greater role for the IMF’s special drawing rights (SDR) as a pathway to gradually replacing existing reserve currencies with a kind of super currency based on SDRs (Zhou Xiaochuan, 2009). The BRIC countries have a total of $1.711 trillion worth of US Treasury Bonds, accounting for 33\% of the total of $3.27 trillion of American overseas debt. Recently Brazil, Russia, and China have begun to put their money where their mouth is and begun to diversify their dollar holdings by buying IMF issued SDR bonds (The Chosun Ilbo, 2009; Brahmr, 2009). Meanwhile India has begun to move out of the dollar in a big way through massive gold purchases (Financial Times, 5 November 2009).

These are no more than initial small steps on a road that, of necessity, will have to be long and slow for the simple reason that the value of the foreign dollar holdings would fall in tandem with their sell offs. China obviously would not want the US dollar to collapse overnight especially not while she is busy buying up commodities and land in the peripheral regions under US imperialist control using the self-same imperialist dollars. Nevertheless, I am suggesting that here we have the first signs of a real \textit{external} limit to the structural power of the US over financial markets.

While globalisation, with the attendant policies of deregulation and liberalisation of financial markets, not only put the international financial markets at the apex of global capitalism, it also vastly increased international trade and foreign investments in hitherto inaccessible areas of the world, including China. There is no doubt that at the level of economic fundamentals,
globalisation was successful in spurring the growth of East Asia and China thereby giving a new lease of life to a moribund world capitalism, but—in so doing—also creating the foundation of a counter hegemonic pole, a rivaling centre that will ultimately challenge the dominance of the US.

**Conclusion: What Next?**

The aim of this paper has been to reflect on the importance of the political economy of the international monetary system in relation to contemporary globalisation. Without a stable international monetary order, economic globalisation creates such a vast space of risks, that the need to reduce, hedge against, and spread these risks inevitably drives capital into the stratospheres of pure circulation. As I have argued in this paper, this is the crucible of financial and economic crises.

The benefits of a global currency seem obvious. If the foreign exchange markets disappeared it would save companies and individuals hundreds of billions of dollars a year in foreign exchange and hedging costs, and it would stabilise international business. There would be no more national currency crises, nor the need to maintain large reserves of foreign assets to counter dramatic fluctuations in the market. But money does not exist in a political vacuum. A global currency would require a unified global political system in which all nations would surrender the last remaining shreds of national sovereignty. No single nation would be able to adjust its domestic monetary policy to remedy a specific domestic economic situation or help its economic agents get a competitive advantage in the globalised economy. This dream world is a long way off and the fact that the G20 Summit in London in April 2009 provided for a $250 billion in SDRs to be distributed by the IMF is a very small step indeed amounting to no more than 4% of the share of SDRs in the total of global reserves. To make the SDRs the principal reserve asset via allocation, nearly $3 trillion in SDRs would have to be created (Reisen, 2009, p. 2). The G20 at its September 2009 meeting did not even bother to address the issue, which testifies to the impossibility of such a scenario in the near or medium term future.

An alternative scenario in which the renminbi replaces the dollar is equally a long way off. Whilst China has recently launched initiatives to promote the renminbi as a regional currency (Business Week, 2009), the consensus in the financial business literature seems to be that China both lacks the depth of financial markets to support reserve currency status, and the will to go down that path in a hurry because it would entail fundamental changes to its growth model. And while at present there is a groundswell of opinion that the renminbi will eventually surpass the dollar as reserve currency, the time lines for this vary from 2020 to 2050. But in international political economy even 10 years is a long time. What is likely to happen in the interregnum?

Some commentators, noting the economic and political frustration of emerging market economies with America’s ‘exorbitant privilege’ as de Gaulle referred to it many years ago, expect that we are heading for a fragmented currency system where countries will opt to hold reserves in a number of rivaling currencies (including the dollar, the Japanese yen, the euro and the renminbi) and gold. Such a system does nothing to remove the problem of instability and volatility in financial markets and, as Cohen (2009) reminds us, the last time the world had experience of it was during the interwar period and the outcome was dismal.

Much depends on whether and how the US is prepared to manage the transition. Even while an orderly decline of the dollar’s supremacy would have many benefits for the US domestic economy (cf. Roubini, 2009), there are also huge costs. First is the loss of so called ‘seignorage’
revenues. These are the net interest incomes accruing to the US Fed from issuing the currency. They amounted to no less than $43 billion in 2008 (Reisen, 2009). Second is the ability to finance deficits in its own currency. But most importantly is the geopolitical hegemony that the dollar’s status helps to support.

And here is the nub. Up until recently, as I have argued in this paper, US hegemony was supported by petro-backed dollars. But in the past 10 years an increasing number of oil producing countries have decided to leave the dollar as the currency of denomination for oil payments in favour of either the euro or a basket of currencies. Notably Venezuela, Iran, and most recently a group of Gulf Arab States (cf. Fisk, 2009). Iraq’s decision, in 2000, to go the same way provoked, according to some observers, the US led invasion of Iraq (cf. Clark, 2003; Iseri, 2009). It would seem, therefore, as Engdahl (2006) points out, that there is nothing now to back up this US reserve status except naked military power. In other words, the dollar’s only remaining role is that of a ‘safe haven’ currency. But this role invites a strategy of military posturing and the creation of permanent crises. The neo-conservative cabal that ran the Bush administration understood this perfectly and opted for a strategy of massive expansion of US military bases world wide including military encirclement of China. The Pentagon’s New Strategic Defense Document of 2005 explicitly fingered China as a potential enemy (Chossudovsky, 2005).

Which way will the Obama administration turn? Will it want to and/or be able to manage a peaceful transition to a global currency or prepare for a violent clash of currency wars and imperialist rivalries? The outlook is pessimistic. While letting the dollar sink, the Obama administration continues to prepare for war. Obama, even as he is awarded the Nobel Prize for Peace, has decided to expand US armed forces and the Pentagon budget rather than shrink the US global mission. But perhaps he can not help it. As Tom Englehardt (2009) puts it in a lucid and comprehensive survey of the American militarised state and economy: ‘War is now the American way’.

Notes

1 There is a widely held neo-liberal view that supports the efficient market hypothesis (EMH) first promulgated by Eugene Fama of the University of Chicago which claims that financial markets price assets precisely at their intrinsic worth given all publicly available information. Hence in this view markets never go wrong and when something does go wrong, individual behaviour is to blame. An interesting fireside comment by Alan Greenspan, former Chairman of the Fed, in a television broadcast in September 2009 summed it up neatly: ‘We will have more crises and none of them will look like this because no two crises have anything in common, except human nature’ (The Independent, 10 September 2009).

2 There has been a relatively small number of economists who have an understanding of limitations of human rationality, of crowd behaviour and of imperfections of markets even though they do not challenge capitalism as an inherently contradictory system (cf. Kindleberger, 1978; Minsky, 1974; Soros, 2008).

3 For the overproduction/underconsumption argument, see Walden Bello (2009). John Bellamy Foster and Fred Magdoff (2009) build on Paul Sweezy and Harry Magdoff’s seminal work on how monopoly capital was transformed into monopoly-finance capital. For an inclusion of all three Marxist causes, see Sy and Tinker (2009) Meanwhile Samir Amin has developed and adjusted his long standing Leninist critique of imperialist oligopolicies to explain the present crisis (Amin, 2009).

4 This is the view of Professor Merton Miller, the Nobel Laureate, who argued that derivatives were essentially created to cope with uncertainty and financial volatility after the end of Bretton Woods and the 1974 oil crisis (Miller cited in Chancellor, 2000, p. 248).

5 In 1981, the head of the Commodity Futures Trading Commission declared that contemplation of delivery was no longer necessary for futures transactions and cash settlement was an acceptable alternative, thereby retrospectively legitimating the eurodollar interest rate futures contract which had already been traded in the Merc for the previous
five years, and opening the flood gates for a plethora of new index futures contracts at a number of exchanges (cf. Chancellor, 2000, p. 246).

6 CDOs vary in structure and underlying assets but basically they are a corporate entity constructed to hold assets as collateral and to sell packages of cash flows to investors. These packages vary in combinations of risk and return (so called different ‘tranches’). In theory, purchasers of CDOs buy a ‘knowable’ probability and bet on the default being at the low end of the possibility within the probability but these expectations in probability terms break down when the overall system becomes unstable.

7 Engdahl (2008b) has turned up an interesting fact laid bare at a Congressional hearing that points to a political stratagem: ‘In recent testimony under oath, Mr Lynn Turner, Chief Accountant of the Securities & Exchange Commission (SEC) testified that the SEC Office of Risk Management which had oversight responsibility for the Credit Default Swap market, an exotic market worth nominally $62 trillion, was cut in Administration “budget cuts” from a staff of one hundred people down to one person. Yes that was not a typo. One as in “uno.” Vermont Democratic Congressman Peter Welsh queried Turner, “...was there a systematic depopulating of the regulatory force so that it was impossible actually for regulation to occur if you have one person in that office? ...and then I understand that 146 people were cut from the enforcement division of the SEC, is that what you also testified to?” Mr Turner, in Congressional testimony replied, “Yes ... I think there has been a systematic gutting, or whatever you want to call it, of the agency and it’s capability through cutting back of staff.”

8 Woodrow Wilson lamented the concentration of credit which resulted from the new legislation, as one frequent citation attributed to him suggests: ‘A great industrial nation is controlled by its system of credit. Our system of credit is privately concentrated. The growth of the nation, therefore, and all our activities are in the hands of a few men who, even if their action be honest and intended for the public interest, are necessarily concentrated upon the great undertakings in which their own money is involved and who necessarily, by very reason of their own limitations, chill and check and destory genuine economic freedom’ (cf. http://quotes.liberty-tree.ca/quote/wodrow_wilson_quote_57f1).

9 There is growing business chatter on the internet regarding this dollar carry trade with the weight of opinion blaming the US administration’s bank bail outs and near zero interest rates policies, and pointing to the dollar’s likely demise. In a recent article in the Financial Times (4 November 2009), Nouriel Roubini has referred to the dollar carry trade as the mother of all carry trades and mother of all highly leveraged asset bubbles.

10 Ben Bernanke (Greenspan’s successor as Chairman of the Fed) has suggested that the persistent, and growing, current account deficit of the US was not a result of feckless American borrow-and-spend consumption habits but the consequence of a ‘global savings glut’, thereby conveniently blaming the Chinese and other East Asian surplus countries for the crisis that was to follow (cf. Morris, 2008, p. 91).

11 Morris (2008, pp. 93–95) makes the point that the dollar’s fall prior to the crisis was also due to real economic trade diversifications, with America’s share of Chinese exports falling to just over 20%, and primary markets for Middle Eastern oil producers, both for exports and imports being in Asia, thereby making the Asian dollar peg redundant.

12 Stiglitz (2009, p. 113) has put forward the arresting argument that because developing countries feel the need to maintain large foreign exchange reserves as their only defence in a world of acute financial and terms of trade instability, they end up, in effect, lending to the developed countries huge amounts of money at low interest rates. He reckons $3.7 trillion in 2007 alone. This is the difference between the lending rate and the interest rate which these countries pay to the developed countries when they borrow from them.

13 A revaluation of the renminbi would slow down China’s economic growth because it would hurt its exports and make a rising renminbi less attractive to foreign investments. For a discussion, see Kaelberer and Wang (2006), and Eichengreen (2009). Also there is the well known Triffin dilemma, named after the Belgian economist who warned the USA as far back as 1960 that reserve currency status in a rapidly rising world economy would entail permanent current account deficits for the reserve currency nation because of the need to maintain liquidity in the international system.

14 A not inconsiderable sum compared with, for example, the total of US arms exports valued at a ‘mere’ $37.8 billion in 2008 (Sipri Yearbook in Shanker, 2009 passim) not forgetting that the US is the leading arms exporter capturing two thirds of the global arms bazaar.

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