International Monetary Reform: What to do Fifty Years after the Collapse of the Bretton Woods System?

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Men will not always die quietly, and in their distress may overturn the remnants of organization, and submerge civilization itself

John Maynard Keynes, *The Economic Consequences of the Peace*, 1919
Key message

• A well functioning, rules-based international economic system needs leadership.

• This is because:
  • no international order can last without the existence of underlying conditions that minimise competition for markets and resources;
  • leadership is necessary to set the path for a new order;
  • countries need to work together to ensure that the divisions/tensions do not remain entrenched.

• In times of crisis the leader pulls countries together to backstop the crisis and support the world economy
  • For example, the US call for the G20 in November 2008.
The risks of no-leadership

• The 1929 crisis: no framework for countries to work together and prevent the contagion.
  • “… British inability and the US unwillingness to assume responsibility for stabilizing the international economic system…” (Charles Kindleberger)

• What was needed:
  • a relatively open market for goods;
  • countercyclical long-term lending;
  • liquidity and policy coordination.

• What happened: beggar-your-neighbour policies
Tangled leadership

• The US: the reluctant leader
  • increasingly unwilling to underwrite the provision of economic stability and international security;
  • from a reluctant hegemon to a disruptive one?

• Europe: the in-between

• China: the game-changer
A ‘sticky’ monetary system

• The dollar continues to glue the world economy together.
• Managed convertibility constraints the RMB internationalisation
  • geopolitics has driven recent shifts in the use and holding of dollars, but only marginally
• Digital currencies?
Exorbitant privilege and fiscal autonomy

• An aspect of the ‘exorbitant privilege’: the ability to run expansionary fiscal policies when a negative shock occurs
  • no adverse reaction of foreign lenders;
  • no significantly higher costs of borrowing.

• The G7 enjoy larger fiscal space than other countries
  • function of countries’ reserve currency status;
  • shield from adverse short-term international capital flows.

• In this paper we use ‘fiscal space’ in a deliberately usual way:
  • max public debt to GDP that a country can sustain trigger an adverse reaction from foreign lenders.
A. Baseline

B. Increasing reserve currency status
A stable IMS requires multilateral cooperation

- To ensure the smooth functioning of the international monetary system:
  - a stronger multilateral financial safety net;
  - enhanced cross-border cooperation between central banks and regulators;
  - cooperation with regional financial arrangements.

- Risk of monetary and financial fragmentation: a zero-sum game.
A stronger multilateral architecture

• Reforms to make the institutional framework more resilient vis-à-vis the changing dynamics of the world economy.

• Enhance policy cooperation on:
  • fiscal policies to stimulate demand and reduce excessive surpluses;
  • regulations to contain financial instability;
  • an international tax framework to remove loopholes;
  • an international ‘green deal’ for environmental sustainability;
  • smart migration policies to mitigate the demographic imbalances in advanced economies.