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Economics

Medicine proves bad for debtors' wellbeing

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George Soros on Globalization

This is an interesting and informative book. It is an essay that seeks to give George Soros's personal perspective on the contemporary world economy, along with his proposals for reforms to remedy the more obvious "deficiencies of global capitalism". As it is written to persuade policy-makers and politicians, it focuses on the practical and eschews the radical. However, reading between the lines reveals many insights from one of the better-known personalities of normally faceless markets.

Soros defines globalisation as "the free movement of capital and the increasing domination of national economies by global financial markets and multinational corporations". He sees globalisation as primarily benign: the private sector is better at creating wealth than the public sector, growing world trade is generally beneficial, and market systems offer more individual and personal freedom. But he is no simplistic market fundamentalist. He believes that the market needs support, that current international institutions do not provide the right sort of back-up, that globalisation creates winners and losers and that the losers need some help. It is not clear whether this help is to be driven primarily by a desire for justice or by enlightened self-interest among the richer nations.

The book's most interesting part is Soros's analysis of financial markets. He takes the view that "financial markets, left to their own devices, are liable to go to extremes and eventually break down". They need regulation. In domestic contexts, this is what governments provide for banks and other institutions. At the global level, the International Monetary Fund has played the role of avoiding major defaults by nations in crisis. There is a fundamental asymmetry in its operation. If you are a debtor nation, you may need to go to the IMF to ask for help and then be forced to take the accompanying medicine in the form of a structural adjustment package (the Washington consensus of privatisation, trade and financial liberalisation, less government expenditure). However, one country's deficit is another's surplus. Creditor countries are required to do nothing. The problem is how to restore flows of capital to the emerging markets and developing countries. A series of financial crises (in Mexico, the "Asian crisis" of 1997-99 and the Argentine debacle) have led to a situation where the capital flows into the emerging economies of the early 1990s have turned into outflows. The US, however, has enjoyed the major inflows needed to finance its huge trade deficit. While the larger world economies are free to follow counter-cyclical policies, the IMF straitjacket forces debtor countries to follow pro-cyclical policies, often with disastrous consequences in terms of employment, health and welfare.

Soros wants the IMF and major central banks to develop some credit-rating policy for sovereign debt and for establishing lines of short-term credit to give flexibility to debtor nations. These would be predicated on "sound" policy but would allow debtors more scope for avoiding crises.

On development, Soros again argues that markets need help because the market will not provide "public goods". The West's recent record in providing international aid has been abysmal: aid has been falling as a proportion of national income and has failed to meet crises and opportunities such as the collapse of the Soviet economy. Soros proposes that the Special Drawing Rights issued by the IMF could be reallocated from rich countries to poor countries. SDRs are "money" created by the IMF to facilitate currency clearing among fund members. But SDRs can be allocated so that poor nations receive more of them to fund investment schemes.

The main problem with these proposals is the US, which is increasingly following a self-interested realpolitik now that its military dominance is unchallenged (although its economic power in terms of world GNP continues to decline). The US has always supported the limited role the IMF has adopted as financial policeman and free-market enforcer.

Keynes argued for the Bretton Woods institutions to have a role more like that suggested by Soros - creating money to help stabilise member institutions. The US wanted none of this. While it will help larger economies, it has not wanted to help the peripheral economies in Latin America and Asia. Soros has no real answer to US self-interest. His conclusion states that the lesson of September 11 is that the US cannot secure its own prosperity or safety without international cooperation. I doubt that George W. Bush believes this. However, the US economy has structural tensions and may well face intractable problems that will force it away from its inward-looking narcissism. The combination of decreasing economic dominance and increasing military activity may be terminal. In the meantime, the European Union should stick up for itself in transatlantic trade disputes and support developing nations on the international stage.

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