

The Challenge of Global Capitalism, The World Economy in the 21st Century- G. M. Gilpin

CAP 1- The second great age of capitalism

The end of the Cold War sparked a debate on the nature of the new world order. Many optimistic commentators believed that when Communist threat disappeared and America remained the only superpower, American values of liberalism, democracy and free markets would have led to an era of prosperity, peace, and international cooperation. On the other hand, more pessimistic commentators believed that the bipolar stability was being replaced by a chaotic multipolar world, dominated by 5 or more powers continuously in conflict.

COLD WAR ECONOMY: the principle foundations of the international economy based on free market and liberalization has been America's international leadership. USA and its allies subordinated potential economic conflict to the interests of political and security cooperation. This facilitated the compromise on important economic differences.

ECONOMY POST COLD WAR: national priorities changed, and countries started to assign higher priorities to their economic national interests. Es. America started a growing economic unilateralism and the ratification of the North American free trade agreement. During the 1990s, regional concerns began to take precedence over North American, trans-Atlantic and Trans-Pacific issues. The close cooperation of previous decades had weakened, and there could be serious negative consequences for world peace and prosperity.

Since 1980 economic issues have become more central to international affairs than at any time. According to some scholars there was a shift from a state-dominated to a market-dominated world. This resurgence of market was a return of pre-world war I era of expanding globalization. During the late 1990s issues arose from economic globalization.

At the end of the Cold was almost every economist and political leader was optimistic and they thought that globalization would have lead to a prosperous world characterized by peace and international cooperation and political democracy. **Globalization thesis:** a global capitalist economy characterized by unrestricted trade, investment flows and the international activities of multinational firms will benefit rich and poor alike. Market has become the most important mechanism in determining both domestic and international affairs. The nation-state has become anachronistic and in retreat.

In the late 1990 negative reactions to globalization arose: the economic problem was the proof that the costs of globalization are greater than its benefits (increase of income inequality, high chronic levels of unemployment, oppression of women).

Evolution of globalization since World war II:

- 1) **TRADE EXPANSION:** it has greatly expanded at an annual rate of 7% from 1948 to 1973 and much more rapidly than the global economic output. Trade in services has significantly increased during recent years.
 - with the expansion of trade also competition has greatly increased: a great number of economies shifted from an import-substitution to an export-led growth strategy.
 - Trade expansion has been facilitated by:
 - Reduction of trade barriers thank to trade negotiation
 - Deregulation and privatization have opened national economies to imports

- Technological advances in communication and transportation have reduced costs on international commerce

Eight rounds of multilateral trade negotiations under the General Agreement on Tariffs and Trade (GATT), have significantly decreased trade barriers.

Despite these developments, most trade takes place among the most advanced economies, most of the less developed world is excluded.

- 2) INTEGRATED INTERNATIONAL FINANCIAL SYSTEM: thanks to the removal of capital controls, the creation of new financial instruments and technological advanced in communication.

- the amount of investment capital seeking higher returns and foreign investments has grown enormously.

- derivatives or repackaged securities play an important role in international finance

The financial revolution has linked national economy closely, increased the capital available for developing countries and accelerated economic development of East Asian emerging markets.

BUT international finance has become the most vulnerable and unstable aspect of the global capitalistic economy (financial flows are short-term, highly volatile, and speculative).

- 3) FDI from multinational corporations: expanded significantly in the late 1980 (In this period globalization came into popular usage). It increased more than trade and economic output. In 1990 FDI outflows between countries increased at an annual rate of 15%. The greatest portion of these investments has been in high tech industries (automobile and information technology). Most of FDI takes place in advanced industrialized countries because firms are attracted to large markets. Only few countries are actually involved.

Multinational corporations and FDI are very important features of the global economy. controlling much of world investment capital, technology and access to global markets, these firms have become major players not only in international economic but in national affairs as well. Multinational firms have become extremely important in determining the economic, political, and social welfare of many nations.

Economic globalization has been driven by political, economic, and technological developments.

Several reforms led to deregulation, privatization, and open national economies.

Countries accepted unrestricted markets because of the failure of Soviet Union system and of the Third's World import-substitution strategy and the conviction that welfare state has become a major obstacle to economic growth.

With the growth of the proportion of world output traded, there was also a change in the pattern of world trade.

- Many less developed countries shifted from exporting food and commodities to exporting manufactured goods and services.

- Advanced industrial economies have been shifting from manufactured exports to export of services.

This restructuring of the entire global economy is economically costly and politically difficult. WHY?

-Intensification of global competition in manufacturing has resulted in unfair commerce (manufacturers from the low-wage industrializing countries).

-Increased job insecurity, unemployment and income inequality.

-Substantial surplus productive capacity in several industrial sectors (es. Automobile manufacture). The world economy is suffering from a glut of manufactured goods. How to resolve this problem?

According to Krugman more expansionary economic policies will reduce surplus. A large part of surplus problem is due to the exaggerated fear of inflation in countries such as Japan and Germany.

The problem of excess capacity in certain sectors will work itself out as supply is reduced to match demand.

There are two schools of thought on the issue of globalisation:

- 1) **Market-oriented position:** it emphasizes the concept of free market and the decrease in the role of the state in the economy. the demise of communism and the increasing integration of national markets have resulted in a global shift towards such market-oriented policies. Many argue that world is moving towards a highly interdependent world economy that will foster prosperity, international cooperation and world peace. According to this vision, the American economic and political system has become the model for the world.
- 2) **Revisionist position:** it emphasizes the concept of economic conflict, trade protection, and the strong role of the state in the economy. An open world economy will produce more losers than winners, so they foresee a world characterized by intense economic conflict at domestic and international level. The clash between capitalism and communism has been replaced by conflict among rival forms of capitalism and social systems represented in regional economic blocs (North America, European Union and Pacific Asia).

The end of the Cold War and economic globalization have coincided with a new industrial revolution. The computer and the rise of internet are transforming almost every aspect of economic, social, and political affairs.

Most observers believe that the information economy have been giving an impetus to the world economy similar to that produced by steam power, electric power and oil power in the past. With the transition from the oil age to the information age, a new economic model based on computers was created. The economics is divided about whether or not computer power represents a technological revolution on the same scale as steam, oil and electricity.

-some economists point out that is difficult to find convincing evidence that that computer has accelerated the rate of economic and productivity growth.

-a growing number of economists argue that investments in computers and information are beginning to have an important impact on economic affairs.

However, long-term effects of the computer and information cannot be determined with any precision until well into the XXI century.

The economic slowdown in both sides of the Atlantic over the last 30 years, have encouraged many to believe that information economy is the cause of their troubles (they believe that the decrease demand of their labours is due to the wide use of computer and increased supply of workers worldwide because of the entry of Eastern Asia economies).

The most important changes of the new revolution:

- 1) Newer knowledge has been produced over the last 30 years than in the previous 5 thousand. Intensified international competition has stimulated scientific and technological innovation.
- 2) New technologies are applicable to a broad array of economic processes.
- 3) Compression of time in innovation, commercialization, and diffusion of a new product.

Some economics argue that rapid technological advance is having a devastating impact on the highly industrialized countries, such as the massive technological unemployment. This shift is linked to the accelerating shift from manufacturing to services (the manufacturing sector accounted 27% of American GDP in 1960, by 1998 its share had dropped to 15%. This means that the same volume of manufactured goods can be produced with a smaller and more productive workforce. The ongoing switch to services has greatly increased job insecurity among Americans. The rise of the service economy has decreased the demand of unskilled workers. Nowadays America has a trade surplus in services and high increase in importing manufactured goods from low-wage industrializing countries. Other economists claim that technological progress meant new and better job for everyone.

Also important in the transformation of world economy has been the redistribution of world industry away from the older industrialized countries toward Pacific Asia, Latin America and other industrialized economies. Although industrialized countries still possess a preponderant share of global wealth and industry, they have declined in relative terms.

After World War II, intellectuals denounced the capitalist developed countries as imperialist and exploitative in the less development countries. For this reason, many LDCs closed their markets and pursued nationalist import-substitution strategies in order to become self-sufficient.

-1970 unsuccessful efforts to establish a New International Economic Order by LDCs.

-1980 they suffered from huge debts and high inflation rates.

-1990 they introduced market-oriented reforms, they started opening their economies to the outside world and pursue export-led growth strategies. The political unity was disintegrated into regional grouping such as ASEAN.

In 1960 the Asian Tigers grew by 6% annually. Also, Malaysia, Indonesia and Thailand grew rapidly. Several Pacific Asia industrializing countries have developed automobile, electronics that have become highly competitive.

In the late 1980 the region became the most dynamic area in the world and important exporters of industrial and high-tech products. Until the 1997 financial crisis, Pacific's Area economic success was impressive.

1980-1990 China experienced a rapid rate of economic growth and became the most important member of the group of rapidly industrializing economies. China has also emerged as a powerful economic and military power because of the declining military importance of Russia.

The relationship between Pacific Asia and Western powers is an important issue facing the international community. For many western political leaders, the economic rise of East Asia represents an unprecedented economic opportunity. On the other hand, many Europeans and Americans believe that competition from low-wage Chinese, Indian and Mexican workers has been forcing down American wages and causing unemployment in Western Europe.

Opponents of globalization argue that there are some disturbing features of the industrial rise of Pacific Asia:

- 1) The diffusion of industry from industrialized to industrializing countries has occurred very rapidly. Many of the advanced technologies are migrating to the industrializing economies.
- 2) Technical advance in communication have facilitated transfer of manufacturing techniques. Firms have accelerated this diffusion combining cheap labour of the South and the most advanced technique of the North.
- 3) Billions of low-wage workers have suddenly entered the world labour pool.

However, most economists reject the "yellow peril thesis". According to Krugman, the economic success of these countries has due to the rapid mobilization of capital and labour and doesn't represent a significant increase in in national productivity levels and their economic success is a one-time event.

With this shift in economic power and international competitiveness economic and political tensions intensify considerably.

On the long-term, the most important development transforming the world economy can be described as a demographic revolution.

- On one hand every industrialized country has experienced a decrease in population growth and is aging rapidly.
- On the other hand, the population in most of the rest of the world has been exploding. The population in developing world is expected to reach 6.5 billion by 2025. This demographic shift will have a profound impact on global economic and political affairs.

Unprecedented population growth in less developed countries constitutes a massive challenge. Economic development of these countries will require huge transfers of capital and technologies as well as maintenance of global markets for their exports.

This could create additional challenges for the industrialized economies themselves. Population decline, on the other hand, is associated with a slower rate of productivity growth; and, of course, the aging of a population entails an increasing burden of retirement and medical costs. As the rate of productivity growth determines the wealth and power of a society, one can project a profound shift during the twentyfirst century in the global distribution of wealth and power away from the older to the newer industrial powers.

CHALLENGE OF ECONOMIC REGIONALISM

Mid-1980: the new regionalism has become a defining feature of the global economy. it differs form the regionalism of 1950-1960. All major economies with the exception of China, Russia

and Japan are members of a regional economic bloc. It has increased considerably the integration of economic activities among regional arrangements.

- The new regionalism was introduced with the Single European Act in 1986. West European integration had increased trade barriers for non-members and USA started multilateral negotiations. Its purpose was to create a politically and economically unified UE.
- The USA decided to support the North America Free Trade Agreement with Mexico and Canada.
- In response to USA and UE Japan started to create a regional economy
- 1986-1993 Uruguay Round to the spread of regional trade agreements.
- 1980 regional agreement proliferated because many countries feared that the UR never succeeded.
- 1990 there were 100 regional agreements.

The expanding new regionalism was a response to the “security dilemma”, in which each region movement attempts to enhance its own competitive position vis-à-vis other regions. Regionalism in 1990 has been accompanied by financial, manufacturing and other forms of economic integration.

There is no single explanation of economic regionalism.

- western Europe: has been motivated by political reasons
- North America: mixed
- Pacific Asia: principally market driven

As the international economy has become more closely integrated, regional groupings of States have increased their cooperation to strengthen their autonomy, improve their bargaining position, and promote other political-economic objectives. In order to survive in an uncertain changing world, states are adapting to the evolving economic, technological and political environment => they want to increase their own relative gains and to protect themselves against external threats.

There are 3 different positions concerning economic regionalism:

- 1) Most of economists believe that economic globalism will triumph over regionalism, because it is an irreversible linear movement. Nations and regions cannot escape the inexorable forces of global unification.
- 2) A minority of economists believe that the end of the Cold War means that the international economy will continue to fragment into regional economic blocs centered on economic dominant powers.

Many observers consider a regionalized world the only realistic alternative to the dangers of economic regionalism and trade protectionism in a world where national rivalries, oligopolistic competition, and state intervention rather than free market are prevalent.

- 3) There is no linear process in which the forces of global economic integration will eventually triumph over economic nationalism and economic regionalism, but the world is unlikely to fragment into regional blocs. Adherents of this position expect that economic globalism and economic regionalism will prove complementary.

Increasing integration of the world by powerful economic and technological forces, has led many observers to believe that the world economy has become unstable and out of control. The integration of world economy has taken place much more rapidly than has development of

capacity to manage a new economic and technological forces. Many of these troubles arise because the world economy is only partially integrated.

There have been only 2 eras of effective governance of the world economy and they have been the most prosperous eras in history:

- 1) Several years just prior World War I. 1880-1914: high points of free trade and economic laissez-faire, economic globalization reached achievements that have not been equaled before. British opted for trade liberalization and the international monetary system based on the classic gold standard, provided prices and monetary stability. Immense British capital export contributed to the unification of world economy.

In the 1930s, powerful states abandoned laissez-faire and started playing a central role in the determination of international commerce=> Great Depression, fragmentation of the world into rival political blocs and outbreak of World War II.

- 2) Immediately followed World War II until the stagflation of the 1970. The Bretton Woods system was established, and trade liberalization was promoted through the GATT. The dollar was assigned an international role.

These were periods of economic growth and international stability, characterized by a coincidence between the interests of the dominant power (GD and USA) and the requirements for creating a liberal world economy.

In 1960 the quality of American leadership deteriorated. Following the end of the Cold War, the US began to pursue more parochial policies and to emphasize regional rather than global solutions. More and more Americans and Europeans questioned the costs of free trade and unregulated financial movements.

During the Cold War the fundamental purpose of the World economy was to strengthen the economies of the Anti-Soviet alliance.

According to most Americans, global economy can be managed only through market principles. BUT, the reality of market triumphant is challenged by many political leaders. Some individuals consider that free trade and the activities of multinational firms threaten livelihoods and communities. Although opponents to a market-governed international economy are less influential than its proponents, their numbers have increased in proportion to the increasing globalization. Economists themselves are deeply divided over the principles that should guide the post-Cold War international market economy.

CAP 2- The Cold War International Economy

The world economy has passed through several phases:

- 1) 1500-1700: age of mercantilism
- 2) from 1815, the end of Napoleonic wars: first great era of economic globalism led by GB
- 3) world war I to world war II: contraction of international trade and economic chaos
- 4) from Bretton Woods, USA tried to revive a global world economy: the economy divided into 2 systems, the Communist economies of the Soviet Bloc and the capitalistic economies of the free world.
- 5) after the Cold war, conflicting national interests increasingly threaten to undermine the cooperation on which the world economy has been grounded.

From the end of World War II to the early 1970s was the most prosperous era in world History. -western Europe grew 4.5% annually and Japan 10% per year. Even URSS enjoyed economic growth.

Economic growth was accompanied by rapid expansion in international trade. Economic interdependence among the capitalist economies grew rapidly.

It was undermined by political and economic factors:

-American leadership and economic policies to promote full employment

-new international rules and institutional environment provided a stable framework.

1970=> the advanced industrial economies settled into a decade-long stagflation characterized by low rates of economic growth, high rates of unemployment and high rates of inflation because of the dramatic slowing of the rate of productive growth in USA and UE.

FOUNDATIONS OF POSTWAR ECONOMIC SUCCESS

Economic factors: - the war had created a large unsatisfied demand in the industrial economies -on the supply side, domestic investments in technologies and research provided a stimulus for economic growth. - people migrated from the countryside to the cities, - opening of markets and expansion of trade => **In short, favourable demand conditions, rapid accumulation of productive factors, and high productivity growth contributed to an era of rapid economic growth.**

moreover, USA assumed the political and economic leadership to avoid a return to the previous disastrous economic conditions of the pre-world war era.

a consensus between USA and Western powers emerged, they supported the economy based on free trade but solving at the same time the distribution problem: governments promised to compensate losers with full employment and social insurance policies. In the early post-war era, national economies were generally closed so governments were free economic policies promoting rapid growth. As economies started to be open after agreements on economic policies, this ability of the government became constrained. The distribution issue was solved by the expanding economic pie. In 1970 the post war consensus started to erode, and the political foundations of an open world economy were weakened.

BRETTON WOODS SYSTEM

The institutional framework of the post-war world economy was constructed at the Bretton Woods Conference in 1944 and reflected American and British thinking. **Bretton Woods Conference established guidelines and institutions for the international economy and permitted governments to pursue economic stabilization and social welfare.** The major economic powers agreed that trade and other economic activities should be regulated by binding rules and the states were not to interfere. This rules were based on several fundamental principles:

- 1) commitment to trade liberalization via multilateral negotiations incorporating the principle of non-discrimination
- (2) agreement that current account transactions should be free from controls but that controls on the freedom of capital movement were permissible
- (3) agreement that exchange rates should be fixed or pegged and that, while an individual nation could modify its exchange rate, it had to consult with the IMF before making major changes.

The original BWS has been repeatedly modified in response to economic and political realities: USA allocated to Western European powers 2% of GDP through Marshall Plan as a buffer to Soviet expansion. Moreover, USA supported EU integration. As a precondition, Europe had to lower barriers to intra-European cooperation.

During the years of the Cold War, the post-war international economic order and the international security order became intimately joined.

Two international regimes embodied in institutions were particularly important:

- 1) **International Monetary System**: it had to provide monetary reserves in sufficient amounts to enable members to maintain exchange rates for their currencies at predetermined values. It used contributions from member countries and offered reserves credits to states with international payment problems. In order to stabilize the monetary international system, the monetary policies of member states were anchored by tying every currency to the dollar, which in turn was tied to gold, and the major powers also informally coordinated their economic policies. this monetary system was successful and lasted until 1970, it was a compromise between the rigid gold standard and the monetary anarchy of the 1930s.

to achieve both autonomy and stability the system was based on some principles:

Fixed exchange rates, reserve credit in the event of an international payment problem, IMF approval of exchange rate adjustments in case of disequilibrium in nation's balance of payment. The American dollar became the keystone of the international monetary system. BUT USA started ceasing to pursue price stability during Vietnam war in 1960, the acceleration of inflation led to the abandonment of the rate fixed system in 1971, by Nixon administration.

The international role of the dollar as a reserve and a transaction currency, became a cornerstone of America's global economic and political position. This conferred to USA the right of seigniorage.

a fundamental contradiction existed at the heart of this dollar-based system: this outflow of dollars meant that one day USA would be unable to redeem in gold and at the agreed price these dollars => this problem became acute in 1960.

During Vietnam war confidence in the value of dollar declined and the Bretton Woods System of fixed rates began to erode and speculation in gold intensified.

By the late 1960 GB pulled away from its close partnership with the USA. Until this moment, the support for the dollar was based on cooperation with the British.

-in 1960 West Germany replaced GB by holding dollars and buying American government securities until 1970 when Germans refused to support Carter economic policies

- in 1980 Japanese replaced Germans through their investments

-in 1990 sporadic informal cooperation among Japan, Germany and USA supported the international role of the dollar : this cooperation continued largely due to fear of what would happen to the international economic and political system if the monetary system were to break down.

GATT: world principal trade organization. The trade regime was born in conflict between USA and GB: Americans wanted to achieve free trade and open foreign markets; British were concerned over the possible loss of domestic economic autonomy. The purpose of the GATT was to promote freer and fairer trade. BUT it was a negotiating forum rather than a true international organization, thus it had no rule-making authority.

The GATT provided a rule-based regime of trade liberalization founded on the principles of non-discrimination, unconditional reciprocity, and transparency.

For these reasons in 1995 the GATT was replaced by World Trade Organisation (WTO) that is a full-fledged international organisation. Under GATT markets were opened and new rules established, GATT's goal was an open multilateralism. The members had to have some criteria and agree to obey the rules.

A significant shift in negotiations took place during the Kennedy Round (1963-1967): GATT members agreed to reduce tariffs on particular products by agreed-upon percentages and made trade-offs across economic sectors.

The next major initiative to liberalize trade was the Tokyo Round (1973-1979): It included significant tariff cuts on most industrial products, liberalization of agricultural trade, and reduction of nontariff barriers. The most important task of the Tokyo Round was to fashion codes of conduct to deal with unfair trade practices. The Round did not resolve the American-European dispute over agriculture, satisfy the LDCs, or stop the noxious proliferation of nontariff barriers that occurred throughout the 1970s.

Trade-liberalizing agreements did enable international trade to grow rapidly.

The BWS had several inherent limitations. Many topics and issues of potential importance had been left vague.

- It didn't have authority to deal with agriculture, services, intellectual property rights or FDI, with customs unions and other preferential trading arrangements which then became major components of international commerce.

- the problems of adjustments in payment imbalances were never resolved.

- increasing importance of the multinational corporations and foreign direct investments transformed the international economy.

Many of the economic activities and economic problems that had become extremely important by the 1980s and 1990s had not been covered by the original GATT framework.

Other developments weakened the system:

- US use of protectionist devices

- decline of US

- increasing number and heterogeneity of the participating players

- as the economies opened, governments found more and more difficult to pursue economic policies of full employment and social welfare

- economists believed that domestic and international realms were independent of one another

Despite its limitations, the BWS resolved the fundamental problems of the world economy (the distribution problem was settled both at national and international level). Until the late 1960s, the issue of national autonomy didn't arise among the major powers because they were largely closed economies.

By the 1980s almost every feature of the Bretton Wood System had changed, was changing or was being changed, these developments created serious challenges for the effective management of the international economy.

1970: several developments challenged the BMW=>

- Escalation of the Vietnam war had caused acceleration in the global rate of inflation=> the American Administration refused to increase taxes and chose to pay for welfare policies through inflationary macroeconomic policies.

- The end of the system of fixed rates because of the intensification of speculative attacks on the overvalued dollar

- Oil crisis in 1973 plunged the world in the Great stagflation

- The slowdown of American productivity

- high rates of unemployment

By the early 1970s, American officials concluded that a substantial devaluation was needed because an high inflation continued to undermine not only the dollar but also the overall trading position of the US. The Nixon Administration believed that they had to force a devaluation on its trading partners=> it imposed a 10% surcharge on imports into the American economy and announced that the surcharge would be removed only after a satisfactory devaluation of the

dollar. America preferred destroying the post-war system rather than carry out domestic deflation measures. This led to the end of the Bretton Wood monetary system. The dollar was substantially devalued in 1971 by the Smithsonian Agreement when other countries accepted to depreciate their currencies.

efforts to develop a new system of stable but adjustable rates failed and at the Jamaica Conference a nonsystem of flexible rates was recognised. This reference range was based on the cooperative and sometimes not so cooperative efforts of the major economic powers to stabilize currency values and international monetary affairs.

1973 oil crisis: the oil boycott resulted in a shift of control over the global petroleum market from the US to the OPEC oil producers, resulting in a decrease in American influence. The increase in the price of oil had an deflationary effect (it withdrew a substantial amount of purchasing power from the world economy) and inflationary effect (it raised prices al almost all goods all around the world). US, UE and Japan, reacted with 3 different adjustment strategies and this led to conflicts.

From 1889 to 1937 American productivity grew at an average of 1.9% annually. This growth accelerated to over 3% between 1937 and 1973. Beginning in the early 1970s the growth fell to a low rate of less than 1%. These developments contributed to growing fears of economic decline and deindustrialisation.

END OF BRETTON WOODS SYSTEM

1) Financial Revolution

A majority of economists believed that a system of flexible rates was needed to delink national economies from one another and thus permit each government to pursue policies promoting full employment.

a minority of economists was very concerned about the potential destabilizing and inflationary consequences of delinking the international monetary system from the anchor of gold.

In 1970 the development of the new financial system accelerated especially thank to the huge OPEC monetary surplus following the oil crisis. the international financial flows had expanded enormously. Despite the shift to flexible exchange rates, domestic and international economic spheres became more closely linked to one another because of financial market integration.

The international financial flow has greatly increased exchange rate volatility especially between the dollar and the yan and mark. This situation may have contributed to the shift toward the New Protectionism that took place in the mid-1970.

The unification of national financial markets encouraged the creation of a single, globally integrated market for corporation ownership and corporate takeover activities.

the increase in international interdependence has had a profound impact on domestic economic policy: it has reduced the capacity to pursue full-employment policies and this has undermined the domestic consensus in support of an open world economy.

Each of the original Bretton Woods institutions was responsible for an exclusive sphere of economic activity; therefore, as those once isolated spheres became more and more interconnected, it became increasingly difficult for those institutions to manage their respective spheres of economic activity.

INTERNATIONAL POLICY COORDINATION

In an increasingly integrated world economy, the actions and policies of one government have an impact on the economic well-being of other countries.

- the Group of 7 started formal coordination of their macroeconomic and the economic policies due to the large monetary imbalances.
- the nature of coordination changed suddenly: focused on American efforts to change the policies of its allies to meet America's economic interests.
- 1978 Bonn Summit: high and low point of coordination policy. locomotive strategy: US, Germany and Japan had to introduce expansionary policies. But this coincided with another oil crisis in 1978-1979, so the other attempts to coordinate national policies were less ambitious.

EUROPEAN REGIONALISM

At the beginning of 1900, Europe was preeminent in almost every aspect of modern industry, technology, and scientific affairs. After the 2 devastating wars and the Great Depression, Europe was reduced in power and influence. By the end of the Cold War the US surpassed Europe in economic, technological, and scientific affairs. URSS became the 2 economy and by the mid-1980 China and east Asia were growing at an incredible pace. Despite its diminishing global power, the achievements of the movements toward European economic and political unification can be only described as extraordinary. Western Europe enjoyed rapid economic growth between 1950 and 1960. The expansion was due to the macroeconomic policies of economic expansion and the massive shift of surplus labour from rural to urban sectors and the huge transfers of capital associated with the Marshall plan. In 1973 the rate of economic growth declined precipitously; Euro sclerosis blanketed the continent. This motivated the nations to follow the course of economic and political unification.

while the goals of integration have been both political and economic, the primary means employed to achieve the goals have been economic. The Treaty of Rome (1957) that led to creation of the European Economic Community (EEC), or Common Market, was a crucial step toward unification. The Rome treaty also provided the foundations of the major institutions. In 1978 agreed to establish the European Monetary System (EMS) and the associated Exchange Rate Mechanism (ERM) and thus created a system of relatively fixed exchange rates among the West European currencies. A major purpose was to isolate western Europe from the disruptive effects of the fluctuations of the dollar. Under the EMS, the West German Bundesbank, with its unwavering commitment to price stability, in effect became the central bank for the EEC.

NEW PROTECTIONISM

A negative reaction to trade liberalization began to develop as early as the 1950s, this opposition accelerated in 1970. As formal tariffs were lowered, informal nontariff barriers were raised, especially on steel, shoes, and textiles. The first barriers in 1971 set quantitative limits on import. The New Protectionism was the effect of fluctuating exchange rates, oil crisis, stagflation, the increasing technological sophistication of Japanese export. It was largely directed against Japan.

it is so named because it is different from older form of protectionism. Whereas the GATT regime was based on explicit rules, multilateralism, and elimination of formal trade barriers, the New Protectionism involved a substantial increase in informal trade barriers, unilateralism, and administrative discretion.

the spread of the New protectionism resulted in part from an important shift in the patterns of world trade: in the early post-war years, intraindustry trade patterns moderated economic

conflict. Since 1970 the situation changed: Japanese trade has been largely interindustry trade, Japanese exports have consisted almost totally of industrial goods, Japanese imports have been largely commodities. US revisionists believed that this was a Japanese strategy of destroying the high-technology industries.

CONSERVATIVE COUNTERREVOLUTION

In the late 1970s monetarism became the dominant macroeconomic theory. It rested on the quantity theory of money and the concept of a natural rate of unemployment. According to this theory, inflation is a monetary phenomenon caused by the creation of excessive money by the central banks. Monetarists argue that government efforts to decrease unemployment below the natural rate will result only in high inflation. Moreover, the solution to different problems is to restrict the role of the government. The doctrine of structural adjustment also became an important component of the conservative counterrevolution. Drastic restrictions of government intervention in the economy was essential to the health of the industrial economies (privatization and deregulation). When Margaret Thatcher came to power as Prime Minister in the United Kingdom and Ronald Reagan as President in the United States, these conservative ideas became political orthodoxy, profoundly reshaped the economic and political landscape, and began to dominate the global economic agenda.

LDC Debt crisis

The mid-1970s were favourable times for many developing countries. In fact, they could borrow directly from American, European and Japanese commercial banks, in this way they could escape the conditions placed on funds borrowed by the World Bank and IMF. The hyperinflation meant that real interest rate was very low.

In 1979 the situation changed dramatically: The Federal Reserve decided to increase interest rates, and LDC found themselves with huge debts and threw them back into dependence upon World Bank and IMF. BUT to receive assistance from them, they had to abandon state interventionism and adopt market oriented economic policies.

The monetarist counterrevolution had a strong political and economic impact: central bankers to wrest control over the economy from "irresponsible" politicians and thus to safeguard national economies from the evils of runaway inflation. In the fall of 1979, the Federal Reserve drastically tightened monetary policy to wipe inflation out of the American and world economies. This courageous action ended stagflation, but it also plunged the world into a severe recession that produced dire consequences, especially for the heavily indebted developing and communist countries.

CAP 3- The Insecure Trading System

Every economist agrees that free trade is superior to all forms of trade protection. Nevertheless, historically protectionism has been more prevalent than has free trade. There has never been free trade with either no or few barriers. For this reason, the term trade liberalization is more appropriate than free trade.

-1846: with the repeal of Britain's Corn Law and the removal of British restrictions on grain imports, the first era of relatively free trade began.

-between WWI and WWII international trade contracted greatly

-following WWII the world experienced another era of trade liberalization

-in mid-1970 global stagflation caused New Protectionism and slowed trade expansion

-at the opening of the 2000, trade liberalization is threatened by intellectual, political and

economic developments.

Although the Uruguay round and the WTO have attempted to deal with these issues, there are substantial problems still confronting the trading system.

Throughout modern history the proponents and opponents of trade liberalization have been engaged in an intense continuous debate.

Proponents: they base their theory on the fundamental principles of the market system formulated by Smith and Ricardo. A country will achieve greater economic efficiency if exports the good for which it has a comparative advantage. Free trade maximizes consumer choice and facilitates efficient use of the world's scarce resources. They argue that the cost incurred by efforts to protect domestic business are very high: a country risks to shut itself off from trade competition. Economists believe that protection of infant industries can be a valid reason for temporary trade protection: if protected from international competition will become sufficiently strong and competitive to enable it to survive even after.

Opponents: the rationale of trade protectionism has changed in important ways.

1) mercantilism 1600-1700: considered manufacturing of great value because of its association with military power and national autonomy.

Causes of protectionism: -economic slowdowns, -public misunderstanding of what trade does, -political process tends to favour special interests.

Several trade developments since WWII have added support to protectionist causes.

Trade increase national wealth, but at the same time it creates losers=> national policy has to assist or compensate workers and others harmed by trade liberalization.

trade neither increases overall employment in an economy (it is determined by fiscal and monetary policies), but at the same time competition shuts down industries that are losing comparative advantage. A nation's trade deficit is mainly due to a low savings rates and not to the unfair behaviour of another country.

Economists have accepted the H-O model has the standard explanation of international trade. This theory postulates that a country will specialize in the production and exports of these products in which it has a comparative cost advantage over other countries. This is determined by the factors such as capital, labour and natural resources. The H-O model has been transformed to include factors such as skilled labour, learning-by-doing technological innovation and economies of scale.

The multinational corporations play an increasing important role, and frequently they don't conform at all to conventional trade theory based on the concept of comparative advantage. The amount of trade resulting from MNC has grown considerably and internationalization of manufacturing is one of the fundamental features of the international economy.

Another important change in international trade theory is represented by the shift from comparative to competitive advantage. According to this theory, historical accident and technological developments have grown in importance in determining trading patterns. A national economy affects the environment of domestic firms in ways that either facilitates or obstruct the development of competitive advantage in certain industries. The advantage in international trade is created by deliberate corporate and governmental decisions and policy choices rather than being a static gift by Mother Nature.

Strategic trade theory

The conventional theory of international trade has been challenged by the development of the **strategic trade theory**: a firm assisted by its own government can design a strategy that will enable it to compete effectively in an oligopolistic industry. This theory is applicable to high-tech sector products as automobiles, computers, and pharmaceuticals. The economies of scale in such industries will lead the market to support only one or just a few large firms, and the market will be dominated by a limited number of firms. The behaviour of one firm will alter the decision of other firms. In a truly competitive market, the new theory would not apply. Oligopolistic firms can and do follow strategies in which they adjust their own prices and output in order to alter the prices and output of competitor firms. 2 of the most important strategies used to increase a firm's long-term domination of an oligopolistic market are dumping and pre-emption of a market. The firm's home government has a crucial role: it can protect domestic firms through subsidies against foreign competitors. According to some economists, strategic trade theory has had an important impact on government policy and has been the factor in the slowdown in the growth of world trade.

BUT, economists find difficult to assess whether government intervention in oligopolistic markets actually works and benefits a particular national firm. Government support for infant economies such as internet has frequently been very successful. Moreover, there is strong evidence that government support for research and development greatly benefits the entire economy.

The Uruguay Round

In 1980 the Bretton Wood System was no longer adequate to deal with the highly integrated world economy. The character of trade itself was changing and trade had become closely entwined with the global activities of multinational firms. US began pressuring European countries to strengthen the multilateral trade system (European integration was perceived as a threat).

the Uruguay Round Agreement in 1995 reduced rich countries tariffs on manufactured goods at very low level and created the World Trade Organization (it was a completion of the framework of international institutions originally proposed at Bretton Woods).

although the WTO replaced the GATT and incorporated many of its rules and practice, it has more extensive rules. It has the primary responsibility for facilitating international economic cooperation in trade liberalization.

- it has much more authority than the GATT: the dispute settlement mechanism was strengthened and establish a new appellate body to oversee the work of the dispute panels.

- the WTO is a membership organization that provides greater legal coherence among its wide-ranging rights and obligations and establishes a permanent forum for negotiations.

- the Round also created a trade-policy review mechanism to monitor member countries' action. thanks to the WTO industrialized countries obtain protection of their intellectual property and access to the markets of industrializing countries. The latter acquired more secure access to the markets of the former.

- the Asia emerging markets will be the greatest beneficiaries of the WTO regime, the less developed economies could experience major losses.

- One of the most important achievements of the Round was creation of the "built-in" agenda for the future activities of the WTO.

there are several issues that deserve further attention:

- intellectual property rights continue to be a source of controversy

- services: even if the Round provides the basic framework for liberalization of trade in services,

many important issues are still unresolved

- agriculture: there are huge obstacles to achievement of free trade in agriculture
- foreign direct investments

The ways in which these important remaining issues are resolved will have a huge impact on the trading system.

New trade agenda: hidden and formal barriers, although trade barriers have dropped over the past half century, they continue to be a major obstacle to the free flow of goods and services. The important remaining barriers are domestic obstacles such as technical standards, administrative discretion. These politically sensitive trade problems include several interconnected social and environmental problems. Economic regionalism represents a new challenge.

Labour standards and Environment protection on one hand powerful groups believe that these issues should be incorporated into the international trade regime. On the other hand, many economists do not agree. The emerging conflict between policies to promote environmental protection and those supporting trade liberalization is of urgent significance. This problem is complicated because some supporters have pressured their governments to use trade measures to promote environmental objectives, others oppose trade liberalization as a threat to national and international environmental standards.

Such experiences have led trade protectionists and environmentalists to ally themselves with one another to oppose trade liberalization. As both trade liberalization and environmental protection are desirable objectives, future trade negotiations must balance the two goals.

Conflicts over labour standards have also become a major impediment to trade liberalization. Most economists reject the idea that labor standards should be incorporated into trade negotiations and argue that the proper venue for such discussion is the International labor organization. The issue of labor standards has been raised by organized labour and by human rights advocates. These proponents of incorporating into trade agreements clauses dealing with such matters as fair labour practices, prohibition of child labour, human rights, and promotion of democracy. China, has been charged with denying fundamental rights to its workers. Most western economies are very dubious about making workers rights a part of the trade regime. The developing countries themselves have denounced efforts to impose western standards because they believe it is a way to reduce the comparative advantage of their economies based on low wage labour. It will be very difficult indeed to reconcile those who support and those who oppose incorporation of workers' rights into the trade regime.

International competition Policy

While globalization has increased competition, it has also led to increased anticompetitive behaviour. The purpose of international cooperation policy (antitrust policy for Americans) is to set the terms for the globalization of business competition. National differences in ICP have become important barriers to trade and foreign investments (US have very strict rules governing the concentration of power). One of the issues to be resolved is the increasing use of the antidumping provision of the GATT as a protectionist advice.

while almost every country has regulations governing domestic cartels, merger activities and unfair business practices, countries differ on matters such as transparency of internal corporate affairs and tolerance for the concentration of corporate power. Such differences cause great difficulties for firms trying to export goods to a foreign market an/or invest in other economies. Therefore, harmonization of competition policy has become a major issue in international trade

negotiations. Even if these differences were not considered important after WWI, with increased interdependence and the integration of trade and FDI, they have become more significant in determining international competitiveness. F.E. the Japanese system of industrial grouping has been criticized by Americans and Europeans because it discriminates against non-Japanese firms and constitutes a major barrier to imports into Japanese market. It has protected mom and pop stores against competition from large Japanese firms and foreign firms in order to preserve neighbourhoods.

2 approaches have been proposed for greater harmonization of competition:

- 1) to establish an international code and rules governing this policy proposed by UE
- 2) international cooperation in the enforcement of either national and regional competition law proposed by US. Both approaches would be difficult to implement because they are joined to a particular society's attitude toward the market and economic matters. And also it is difficult to determine if a policy is intended to promote domestic welfare or to keep out foreign competitors.

The inability to agree on international cooperation in this area has contributed to the development of managed trade and regional agreements, which contains its own definition of fair competition.

Regionalization is a challenge to the WTO trade regime. 1980-1990 regional pacts expanded until they covered much of the world trade. During the first decades of post-war period, such regional arrangements reinforced economic multilateralism. BUT their proliferation has raised concerns for different reasons: 1) regional trading blocs tend to discriminate against non-members, 2) new trading customs increase costs, 3) regional arrangements enable grouping of states to attract FDI by MNCs.

The WTO should ensure the compatibility of regional arrangements with continuing multilateral trade. At the opening of the new century, WTO have not been effective in dealing with protectionist tendencies of regional arrangements.

The international trade organization has been assigned a mandate to regulate competition policy. with no international agreement on competition policy, efforts to achieve harmonization have focused on the regional level.

WTO: the creation of the WTO was a major achievement in resolving trade disputes, but it suffers from serious resource constraints both in funding and personnel.

The GATT was governed by a small executive council whose membership included all the major trading economies: decisions were made on the basis of weighted votes. The US was able to exercise a leadership role.

The WTO is directed by a council composed of all members of the organization, however, the major powers have resorted to an extra-legal process outside the WTO. Uruguay Round signatories unstructured the WTO to cooperate with the IMF, the World Bank to follow consistent and mutually supportive policies. But given the resources this is unlikely to succeed. The huge number of trade issues and of the players, mean that the WTO is already facing an immense challenge. The increase in the responsibilities of the WTO has caused many American and other observers to fear that the WTO's mandate violates the national sovereignty of its members. Every country, in fact, has the right to withdraw from the WTO if it infringes national sovereignty. WTO system of simple majority voting could lead to rewriting trade laws to the disadvantage of the major economic powers. WTO decisions must be accepted by a member state before they can be applied to that state. there is no way to compel a state, US for example, to comply with WTO decisions. Moreover, although a decision by majority vote is possible, the

procedures of the organization are structured in such a way that the big powers can block any significant decision with which they disagree. Therefore, it is more likely that the WTO will be ineffective than that it will threaten the national sovereignty of the United States or any other country. The number of GATT/WTO members has increased from twenty-three to one hundred thirty-two in the late 1990s, with about thirty additional states wishing to join.

CAP 4 - The Unstable Monetary System

A stable and well-functioning international monetary system is in everyone's interest. It is closely tied to the international finance system. Flows of international capital and foreign investment are conducted in money. Like the international monetary system, the international finance system is very vulnerable and can cause international economic turmoil. Monetary instability and financial disturbance can have a disruptive impact on individual lives and on global economies. The international monetary and international finance systems have had an increased impact on one another. Since the breakdown of the system of fixed exchange rates, there has been no stable and satisfactory international monetary system.

Technical mechanisms are seldom politically neutral, they affect the economic welfare, political autonomy, international prestige of individual states. Every state wants a well-functioning monetary system, however, they can disagree on such matters as currency values and the precise mechanism to be employed to solve technical problems. A well-functioning monetary system requires a strong leadership by a nation or a group of nations which has to assume the initiative in solving technical problems and in providing financial assistance. Leadership has historically been provided by a dominant economic and military power: GB and US. The rules governing the monetary system have reflected the interests of these leading countries. Since the early 1970s the area of international monetary system has been the focus of very intense controversy among economists. The monetary system's inherent problems and contradictions remain unresolved.

Adjustment problem

an international monetary regime must determine the method by which national economies will restore equilibrium. Every adjustment policy results in economic costs, an efficient monetary system should reduce that costs.

When a country has an imbalance in its international payments:

- 1) to change an exchange rate by devaluing (deficit country) or appreciating (surplus country) the currency.
- 2) to shift to deflationary (deficit) or expansionary (surplus) economic policies.

Such national differences in inflation/deflation rates will cause currency values to change. For every deficit country, there must be one or more surplus country.

while either the deficit or surplus country could make adjustments, the burden of adjustment rested with the deficit country. However, the deficit country takes actions to impose the costs on the surplus country. Adjustment for a deficit country, means that it must reduce its standards of living, achieve a long-term reduction in national income (devaluation) and reduce employment levels (deflation). For a surplus country, appreciation is painful for its export industries, while beneficial to its importers and consumers. **EXAMPLE:** 1980 clash between deficit US and surplus Japan. Japanese agreement at the Plaza Conference (September 1985) to appreciate the yen was achieved only after intense American pressures. Thus, adjustment mechanism reflects the interests of powerful states and groups.

Liquidity

An efficient international monetary system must also provide international liquidity. Countries must have financial reserves for:

- 1) to meet balance of payments deficit caused by economic shock and increase the time and options available to the country as it seeks a longer-term solution.
- 2) to delay a possible costly devaluation of its currency

Neither under provision (high levels of unemployment) nor overprovision (this means high level of inflation such as during the era of dollar standard) is desirable for world economy's functioning. The dominant powers have had a strong impact on maintaining the level of international liquidity to accord with their interests.

An important aspect of liquidity creation is seigniorage for the country which supplies the primary international currency:

Advantages: national prestige, major source of increased income to the nation, increase in economic and political autonomy because it is freed from balance of payment constraints. The banking system supplying an international currency enjoys both economies of scale and other costs advantages over its competitors because transactions are held in its national currency. Even after the Cold War, for years the role of the dollar as the world's key currency permitted the United States to live far beyond its means and thus to become the world's foremost debtor nation. As the American debt has been denominated in dollars, this debt burden could be inflated away, and devaluation of the dollar in the 1990s did indeed reduce the debt owed by the United States while simultaneously imposing heavy costs on Japanese and other lenders.

Costs: it has to pay interests to other countries holding assets denominated in its currency and it can find difficult to devalue its value.

As long as there is no acceptable alternative, the US will continue enjoying the privileges of seigniorage.

A stable international monetary system is also dependent on the confidence problem: the countries must have the confidence that the reserve-currency country will not pursue inflationary policies leading to devaluation of their own reserves. If they lose confidence, other countries will shift the composition of their reserves. A shift can also occur because of changes in the interest rate paid on assets denominated in a currency, changes in exchange risk, or inflationary concerns.

Some may lose more or benefit less than other from a monetary arrangement; strong reactions can be evoked. Es. Many Europeans objected to the US privileges and its inability to reduce its trade deficiency by devaluing the dollar.

Intellectual disagreements exist among economists about many possible solutions to the technical issues embedded in a monetary system. At the heart of difficulties there is the fact that national economies have very different rates of inflation and price instability. Germany and Japan gave more importance to price stability, US pursued inflationary policies. Moreover, nations may want at the same time fixed exchange rates, national independence in macroeconomic policy and capital mobility (trilemma or irreconcilable trinity). BUT the international system can incorporate at most 2 of the desirable but irreconcilable goals. Different countries and different groups prefer emphasizing different goals (US- independent monetary policy and freedom of capital, UE-fixed rates, China- macroeconomic independence). Specific economic interests also differ in their preferences. As national situations and interests differ, there is no solution to the trilemma that would be satisfactory for all.

The trade-off between international monetary system and domestic economic autonomy has

existed for a very long time. 1) first effort to solve the problem was the creation of the Classic Gold Standard under British leadership, there was monetary stability but no control on domestic economies. – 1930-1940 anarchy period, - after WWII fixed exchange rates with sacrificed freedom in capital movement.

Since the breakdown of fixed exchange rates in the 1970s, there has been a non-system of flexible exchange rates. No system: the international monetary affairs are not governed by any rules. The system may be characterized as a reference range system, so named because the central banks of the three dominant monetary powers have cooperated to keep their exchange rates aligned and to maintain monetary stability. This system represents the triumph of central bankers over national governments. However, many critics have denounced this as the cause of high unemployment and even of the economic crisis of the late 1990s. Some economists believe that this system is threatened by several problems such as erratic currency fluctuations, huge imbalances between surplus countries and deficit countries and frequent Japanese and US attempts to manipulate currency values in order to increase the international competitiveness of their industries. Proponents of international monetary reform focus on one or other goals called the irreconcilable trinity. Most economists believe that is necessary either to return to a system of more or less stable exchange rates or to make floating flexible rates more workable.

The advocates of a return to more stable exchange rates assert that the experiment with flexible rates has failed: they have resulted in excessive currency and price volatility, increasing uncertainty and risk in both international trade and foreign investment. Some have concluded that floating rates impose high costs in economic growth and in efficient allocation of economic resources. And they argue that unstable exchange rates have at least contributed to trade protectionism. Fixed rates, on the other hand, are believed to facilitate competition based on comparative advantage and efficient capital flow. They are aware that it is impossible a return to Bretton Wood system because of the huge and speculative international movements of capital. So, they look at a compromise between international stability and policy flexibility.

Proponents of more flexible rates believe that when a government faces a balance of payments disequilibrium, it is far better to devalue its currency than to deflate its economy. The value of the currency acts as a balancing mechanism for the rest of the economy. Many argue that the costs of floating rates have been exaggerated and fixed rates make adjustments more costly and more difficult. According to some scholars the conditions for a system of fixed rates no longer exist. A stable and efficient monetary system must be flexible and robust enough to contain market pressures. The system must have also the capacity to contain market pressures, especially speculative capital flows through imposition of capital controls and intervention of central banks to defend currencies under serious attacks. Although Bretton Woods system succeeded in doing this, future fixed-rate system will not be able to do so because of changed circumstances.

- 1) the institutionalized structure of labour market associated with the welfare state which restrict the fluidity with which prices and wages can adjust to economic shocks
- 2) politization of macroeconomic policy has eroded the credibility of government policies
- 3) increased mobility of capital movements

In these conditions the international monetary system has just 2 options available:

- 1) a regime based on flexible rates
- 2) to create a single currency, as the EU has done

Because the balance of power has shifted from individual nation-states towards currency traders and international financial speculators.

Public officials and economists continue to search for a compromise that will achieve both currency stability and policy flexibility. The main proposals are: **monetary hegemony, an international monetary authority, and international policy coordination.**

1) **Monetary hegemony:** some individuals advocate a return to strong leadership by one country as the most desirable solution to the problem of monetary instability. American hegemony in monetary affairs could be re-established. BUT the dollar will face competition from the euro. The relative decline of the American economy and the fluctuating value of the dollar also make renewal of unchallenged American monetary pre-eminence unlikely. The hegemony of the dollar is clearly over, it must share the stage with euro and the yen.

2) **International monetary authority:** John Williamson has proposed that this authority should be an executive council lodged in the IMF. It would have the responsibility for keeping the exchange rate of states within certain parameters. Under Williamson's scheme countries would preannounce bands within which their exchange rates could vary, and each nation would specify a central rate with a 10 percent margin up and down. This compromise system would retain flexibility and would be more stable than managed floating rates. In the opinion of many economists it is unable to solve the problem of international monetary non-system.

3) **International policy coordination:** IPC is a process whereby individual countries change their economic policies in a mutually beneficial manner. The formal coordination characterized the early years of the Bretton Woods System. In 1994 the Bretton Woods Commission proposed that IPC should be increased. The IMF would assume primary responsibility for strengthening macroeconomic policies, furthering macroeconomic convergence among the major economies, and establishing a formal system of policy coordination. – in the mid-1970s US and trading partners cooperated in recycling OPEC surplus. However, IPC was not a success at the Bonn Summit (1978) and Plaza Agreement (1985). Although the technical problems associated with IPC are formidable, the political problems of coordinating the economic policies of sovereign states are even more challenging. Most importantly, national governments and central banks are extremely reluctant to surrender policy autonomy. A strong state-centric mentality pervades the economic thinking of almost every government. According to Gyohten, a formal coordination requires a strong and willing hegemon. The US no longer appears to have the will or the ability to lead that it possessed earlier. Also, its partners are less willing to follow than in the past. Thus, an institutionalized solution to the problems of the international monetary regime is impossible, because market forces have become too powerful and states too unwilling to make the sacrifices necessary to achieve a coordinated solution to the problems of international monetary affairs. This development could lead to creation of currency blocs based on the euro, the dollar, and possibly the yen; such potentially competitive blocs could fragment the international monetary system and greatly complicate the management of the global economy.