



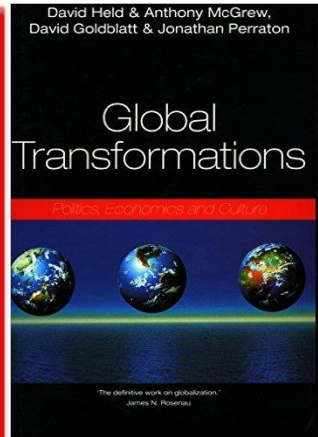
# 5

## Globalization(s) and the evolution of the international monetary system





# D. Held, A.G. McGrew, D. Goldblatt, J. Perraton, *Global Transformations*, 1999



“**Globalization** can be located on a **continuum** with the **local, national and regional**. At one end of the continuum lie social and economic relations and networks which are organized on a **local and/or national basis**; at the other end lie social and economic relations and networks which crystallize on the **wider scale of regional and global interactions**. Globalization can refer to those spatial-temporal processes of change which underpin a transformation in the organization of human affairs by **linking together and expanding human activity across regions and continents**”.

“A process ... which embodies a transformation in the spatial organization of **social relations and transactions** – assessed in terms of their **extensity, intensity, velocity and impact** – generating transcontinental or interregional **flows and networks** of activity, interaction, and the exercise of power”



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# Globalization in a “Issues Brief” of the FMI (2008)

[www.imf.org/external/np/exr/ib/2008/053008.htm](http://www.imf.org/external/np/exr/ib/2008/053008.htm)

“A perennial challenge facing **all of the world's countries**, regardless of their level of economic development, is achieving **financial stability, economic growth, and higher living standards**. There are many different paths that can be taken to achieve these objectives, and **every country's path** will be different given the **distinctive** nature of **national economies and political systems**.

Yet, based on experiences throughout the world, **several basic principles** seem to underpin greater prosperity. These include investment (particularly foreign direct investment), the spread of technology, strong institutions, sound macroeconomic policies, an educated workforce, and the existence of a market economy. Furthermore, **a common denominator which appears to link nearly all high-growth countries together is their participation in, and integration with, the global economy”**.



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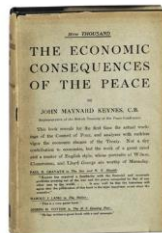




# The «Economic Eldorado» of the *belle époque* (1870-1914)

J.M.Keynes, *Economic Consequences of the Peace*, 1919, CWJMK 2, p. 6

“What an **extraordinary episode in the economic progress of man** that age was which came to an end in August, 1914! ... The inhabitant of London could order by telephone, sipping his morning tea in bed, the various **products of the whole earth**, in such quantity as he might see fit, and reasonably expect their early **delivery** upon his doorstep; he could at the same moment and by the same means adventure his wealth in the **natural resources and new enterprises of any quarter of the world**, and **share**, without exertion or even trouble, in their **prospective fruits and advantages**; or he could decide to couple the security of his fortunes with the good faith of the **townspeople of any substantial municipality** in any continent that fancy or information might recommend. He could secure forthwith, if he wished it, cheap and comfortable **means of transit** to any country or climate without passport or other formality, could despatch his servant to the neighboring office of a bank for such supply of the **precious metals** as might seem convenient, and could then **proceed abroad to foreign quarters**, without knowledge of their religion, language, or customs, bearing coined wealth upon his person, and would consider himself greatly aggrieved and much surprised at the least interference ...



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# The «Economic Eldorado» of the *belle époque* (1870-1914)

J.M.Keynes, *Economic Consequences of the Peace*, 1919, CWJMK 2, p. 6

... But, most important of all, **he regarded this state of affairs as normal, certain, and permanent**, except in the direction of further improvement, and **any deviation from it as aberrant, scandalous, and avoidable**. The projects and politics of militarism and imperialism, of racial and cultural rivalries, of monopolies, restrictions, and exclusion, which were to play the serpent to this paradise, were little more than the amusements of his daily newspaper, and appeared to exercise almost no influence at all on the ordinary course of social and economic life, **the internationalization of which was nearly complete in practice**".



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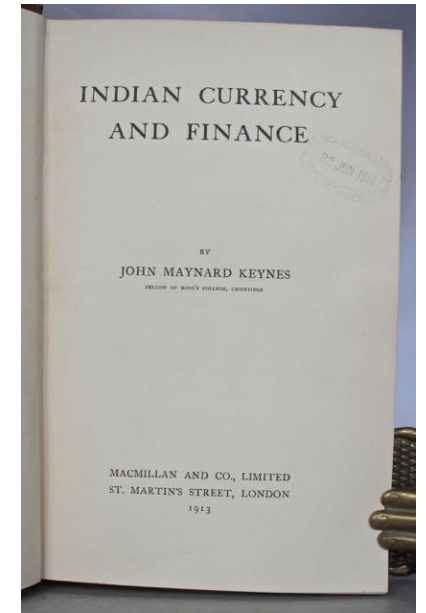


# John Maynard Keynes

Keynes was a **British** economist and one of the most influential of the 20th century.

John Maynard Keynes was born on 5 June 1883 in **Cambridge** into a well-to-do academic family. His father was an economist and a philosopher, his mother became the town's first female mayor. He excelled academically at Eton as well as Cambridge University, where he studied mathematics. He also became friends with members of the **Bloomsbury** group of intellectuals and artists.

After graduating, Keynes went to work in the **India Office**, and simultaneously managed to work on a dissertation - often during office hours - which earned him a fellowship at King's College. In 1908, he quit the civil service and returned to Cambridge. Following the outbreak of World War One, Keynes joined the treasury, and in the wake of the Versailles peace treaty, he published ***The Economic Consequences of the Peace*** in which he criticised the exorbitant war reparations demanded from a defeated Germany and prophetically predicted that it would foster a desire for revenge among Germans. This best-selling book made him world famous.



# THE BLOOMSBURYS

## THE WRITERS



Lytton  
Strachey



Virginia  
Woolf



EM  
Forster

## THE THINKERS



Saxon  
Sydney-Turner



Leonard  
Woolf

## THE ARTISTS



Duncan  
Grant



Vanessa  
Bell



Roger  
Fry

## THE ECONOMIST

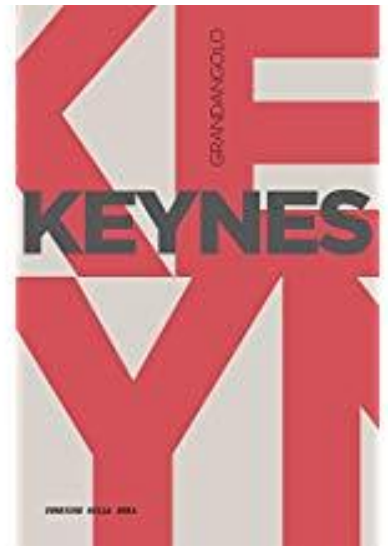
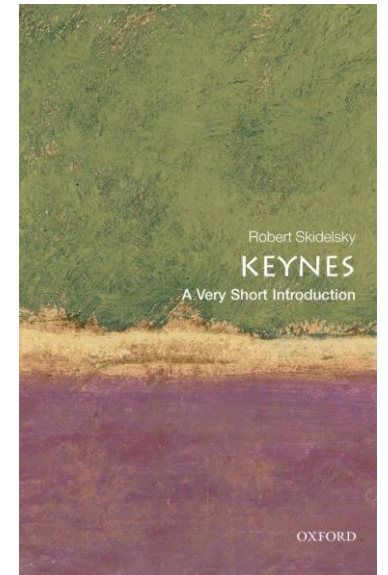


John Maynard Keynes

## THE ART CRITIC



Clive  
Bell





# John Maynard Keynes

During the inter-war years, Keynes amassed a considerable personal fortune from the financial markets and, as bursar of King's College, greatly improved the college's financial position. He became a prominent arts patron and board member of a number of companies. In 1926, he married Lydia Lopokova, a Russian ballerina.

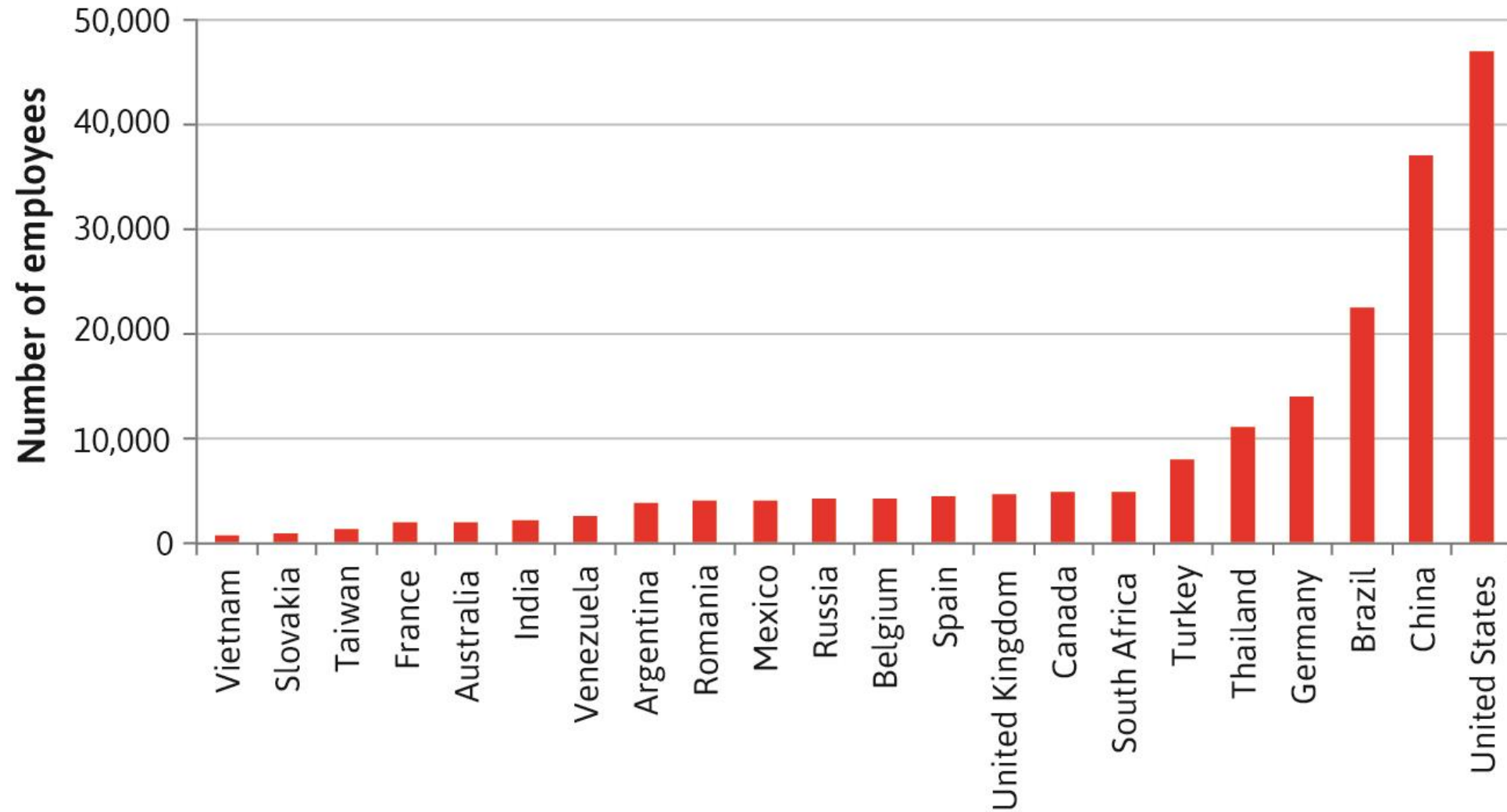
Keynes' best-known work, *The General Theory of Employment, Interest and Money*, was published in 1936, and became a benchmark for future economic thought. It also secured his position as Britain's most influential economist, and with the advent of World War Two, he again worked for the treasury. In 1942, he was made a member of the house of lords.

During the war years, Keynes played a decisive role in the negotiations that were to shape the post-war international economic order. In 1944, he led the British delegation to the **Bretton Woods** conference in the United States. At the conference he played a significant part in the planning of the World Bank and the International Monetary Fund. He died on 21 April 1946.

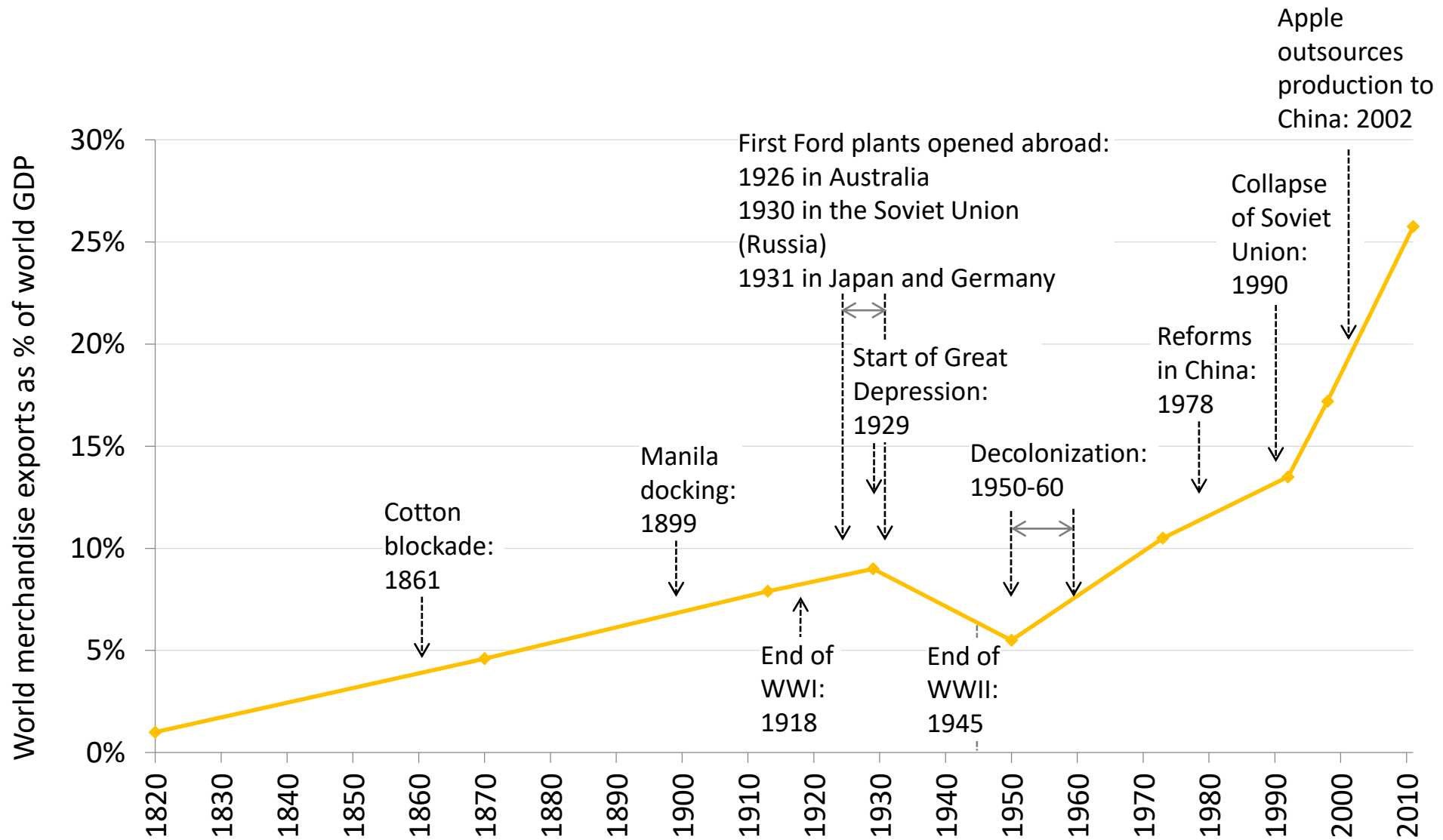




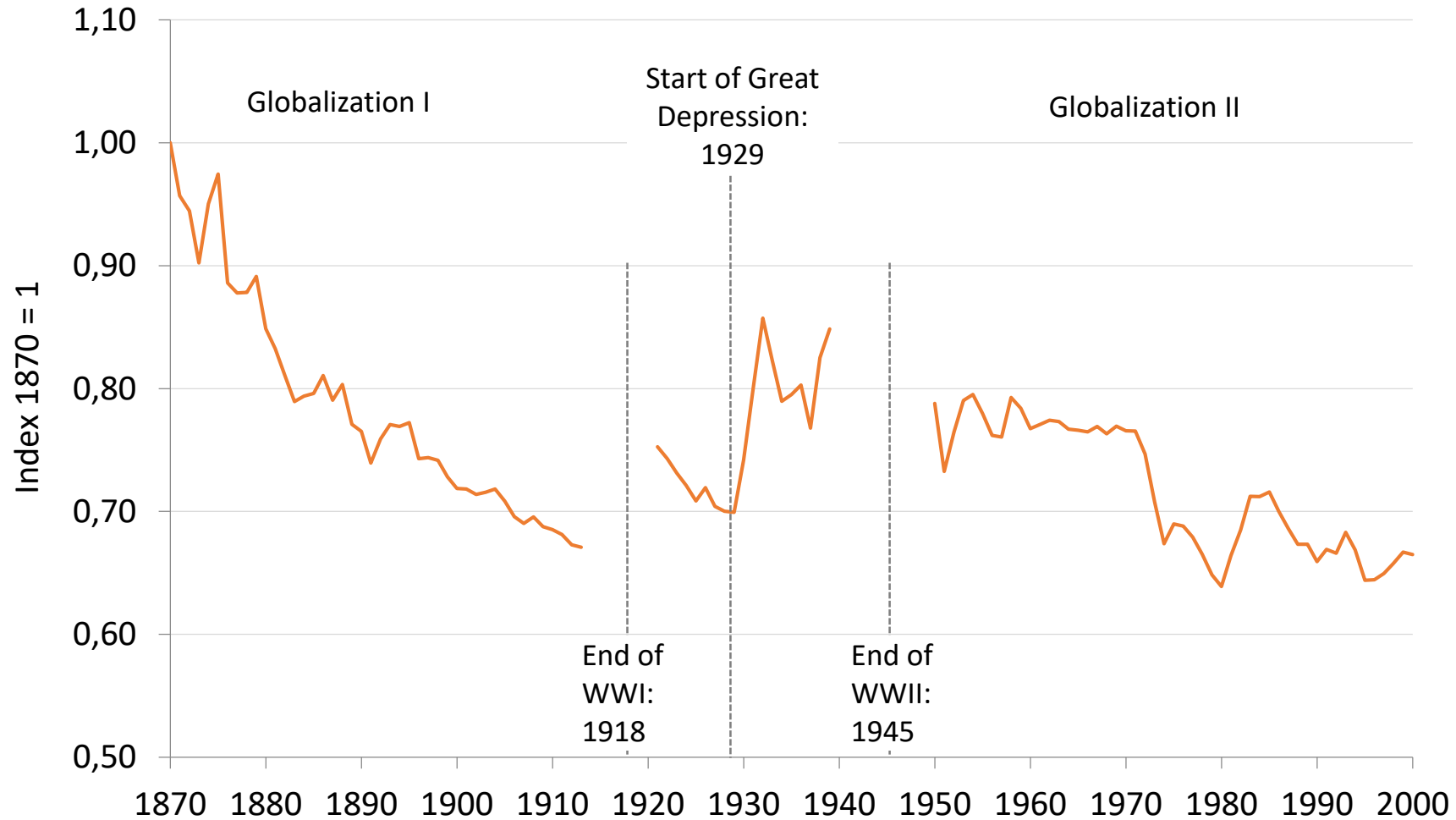
# An «American» company? Ford employees in 2016



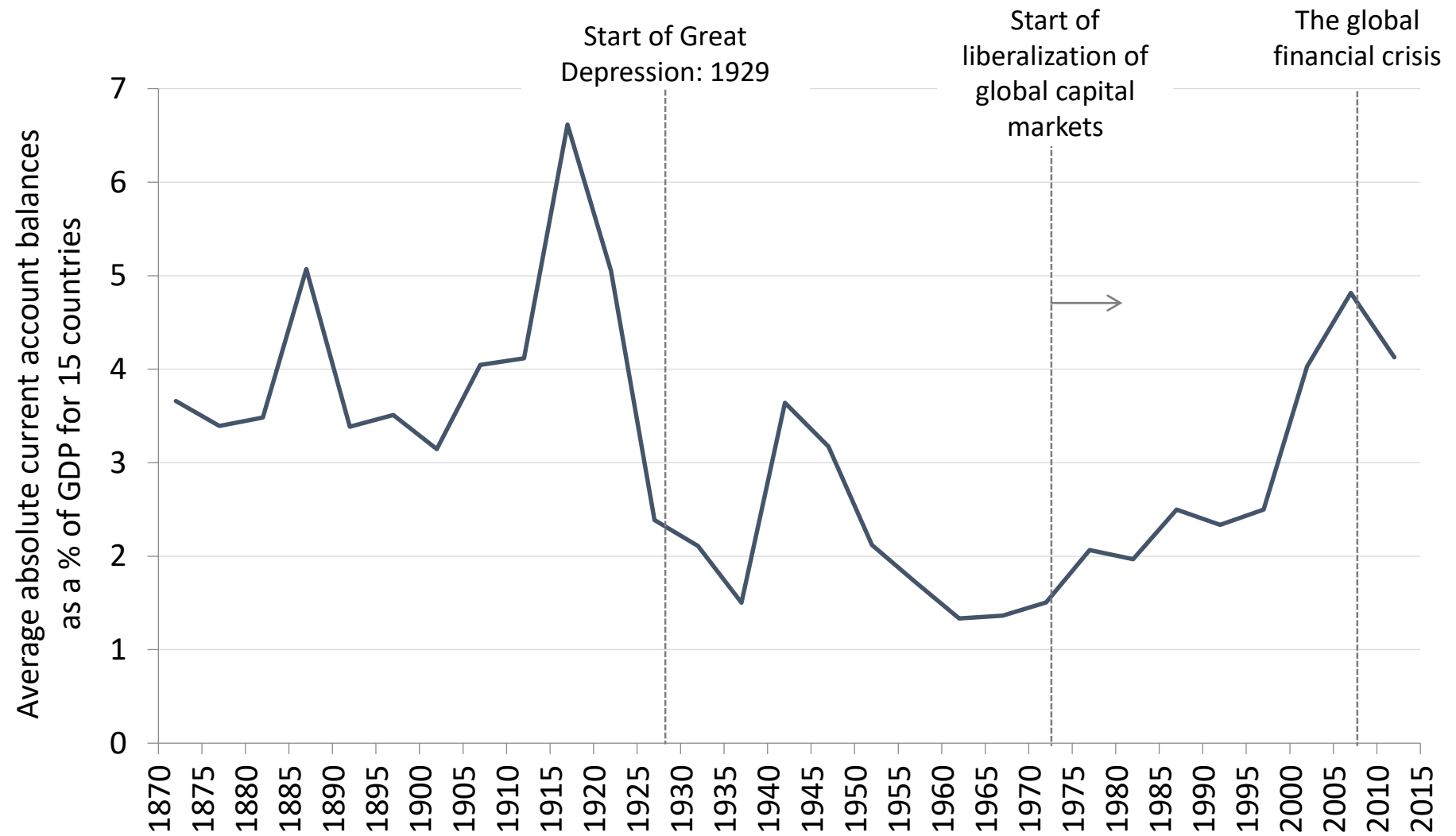
World merchandise exports as a percentage of world GDP (1820-2011) [Source: Core Econ, *The Economy*, ch 18]



Impediments to trade (1870-2000) [Source: Core Econ, *The Economy*, ch 18]

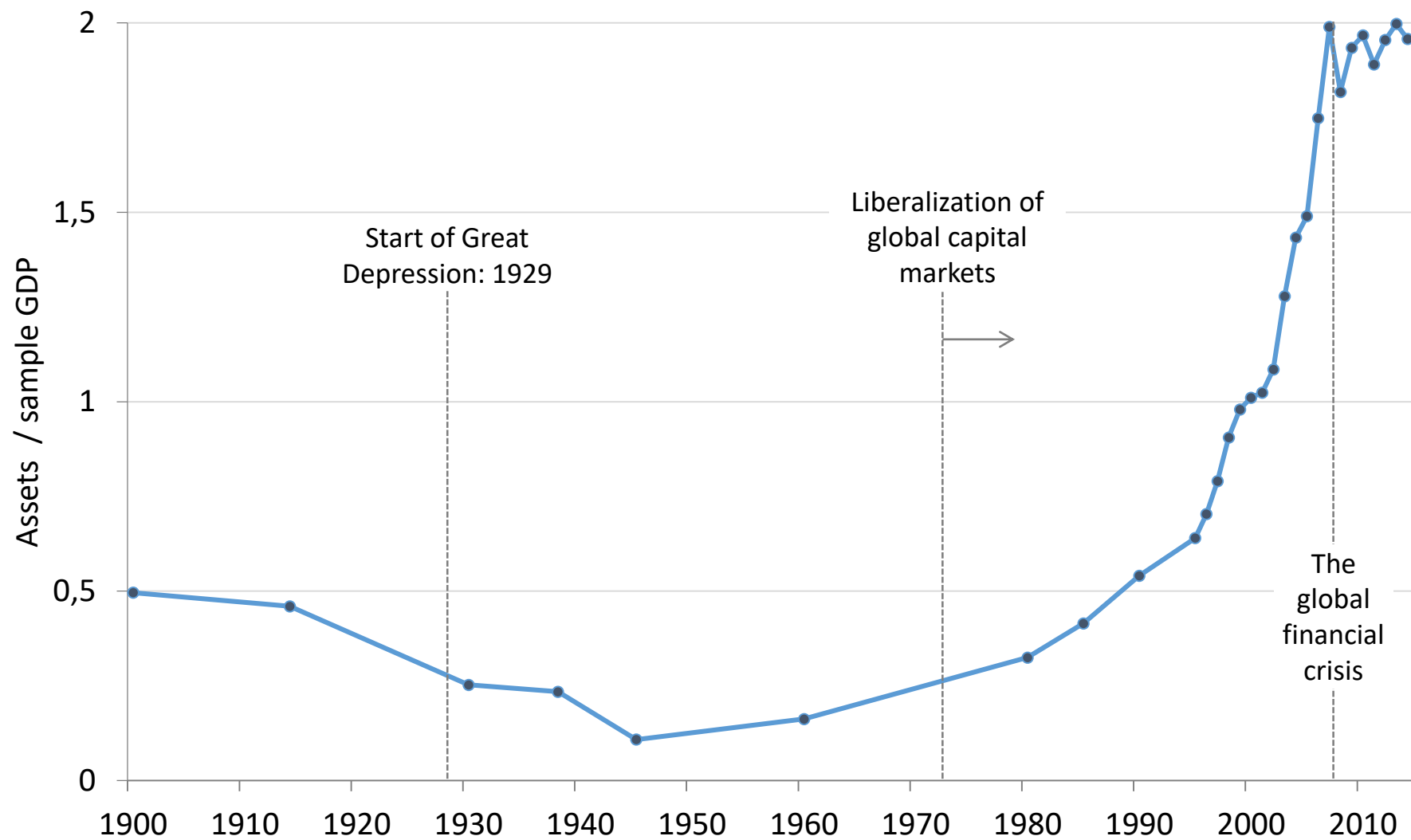


# International capital flows (1870-2014) [Source: Core Econ, *The Economy*, ch 18]





International asset holdings (1900-2014) [Source: Core Econ, *The Economy*, ch 18]



*[From Mankiw, Essential of Economics, chapter 13, Saving, Investment, and the Financial System]*

$Y = C + I + G + NX$  -  $Y$  is total income (GDP), is divided into four components:  $C$  = consumption;  $I$  = investment;  $G$  = government spending; and  $NX$  = net exports

**Closed economy** - 'one that does not interact with other economies (excludes international trade)  $Y = C + I + G$  'Each unit of output sold in a closed economy is consumed, invested, or bought by the government'

$Y - C - G = I$  - total income that remains after consumption ( $C$ ) and government expenditures ( $G$ )

**National saving** ( $S$ ) =  $S = Y - C - G$ ; so  $S = I$  or savings equal investment

$S = (Y - T - C) + (T - G)$  where  $T$  = government taxes - national savings is separated into two components, e.g., *private saving* ( $Y - T - C$ ); and *public saving* ( $T - G$ )

**Budget surplus/budget deficit** - 'If  $T$  exceeds  $G$ , the government runs a ***budget surplus*** because it receives more money than it spends .... If the government spends more than it receives in tax revenue, then  $G$  is larger than  $T$  ... the government runs a ***budget deficit***, and public saving  $T - G$  is a negative number.'

$S = I$  'For the economy as a whole, saving must be equal to investment' '...investment refers to the purchase of ***new*** capital, such as equipment or buildings'

**Slides 15 to 23:** borrowed from <https://personal.utdallas.edu/~dxs093000/Macro/chap5.pdf> (chapter 5 of G. Mankiw, *Macroeconomics*, 6<sup>th</sup> edition).

# In an open economy,

- spending need not equal output
- saving need not equal investment

## Preliminaries

$$\mathbf{C} = \mathbf{C}^d + \mathbf{C}^f$$

$$\mathbf{I} = \mathbf{I}^d + \mathbf{I}^f$$

$$\mathbf{G} = \mathbf{G}^d + \mathbf{G}^f$$

superscripts:

$d$  = spending on  
domestic goods

$f$  = spending on  
foreign goods

$\mathbf{EX}$  = exports =  
foreign spending on domestic goods

$\mathbf{IM}$  = imports =  $\mathbf{C}^f + \mathbf{I}^f + \mathbf{G}^f$   
= spending on foreign goods

$\mathbf{NX}$  = net exports (*a.k.a.* the “trade balance”)  
=  $\mathbf{EX} - \mathbf{IM}$



GDP = expenditure on  
domestically produced g & s

$$\mathbf{Y} = \mathbf{C}^d + \mathbf{I}^d + \mathbf{G}^d + \mathbf{EX}$$

$$= (\mathbf{C} - \mathbf{C}^f) + (\mathbf{I} - \mathbf{I}^f) + (\mathbf{G} - \mathbf{G}^f) + \mathbf{EX}$$

$$= \mathbf{C} + \mathbf{I} + \mathbf{G} + \mathbf{EX} - (\mathbf{C}^f + \mathbf{I}^f + \mathbf{G}^f)$$

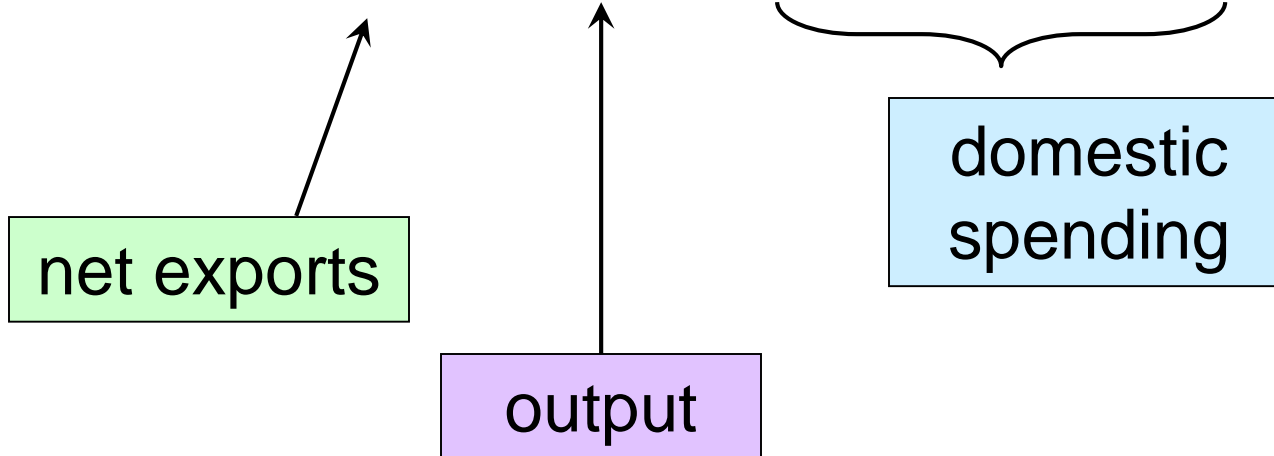
$$= \mathbf{C} + \mathbf{I} + \mathbf{G} + \mathbf{EX} - \mathbf{IM}$$

$$= \mathbf{C} + \mathbf{I} + \mathbf{G} + \mathbf{NX}$$

The national income identity  
in an open economy

$$Y = C + I + G + NX$$

or,  $NX = Y - (C + I + G)$



## Trade surpluses and deficits

$$\mathbf{NX} = \mathbf{EX} - \mathbf{IM} = \mathbf{Y} - (\mathbf{C} + \mathbf{I} + \mathbf{G})$$

- **trade surplus:**

output > spending and exports > imports

Size of the trade surplus =  $\mathbf{NX}$

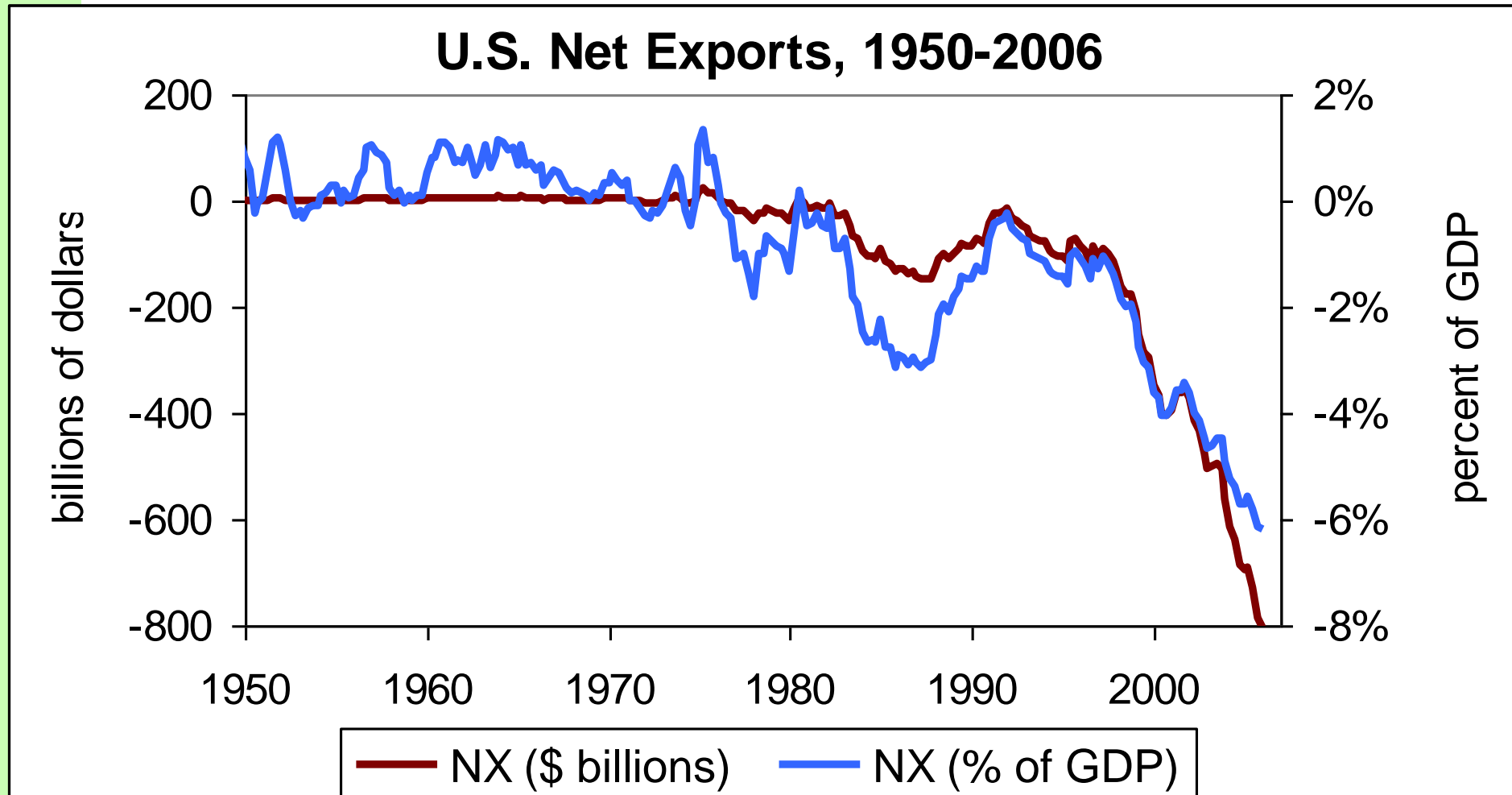
- **trade deficit:**

spending > output and imports > exports

Size of the trade deficit =  $-\mathbf{NX}$



# U.S. net exports, 1950-2006





# International capital flows

- **Net capital outflow**

$$= \mathbf{S} - \mathbf{I}$$

= net outflow of “loanable funds”

= net purchases of foreign assets

the country's purchases of foreign assets

minus foreign purchases of domestic assets

- When  $\mathbf{S} > \mathbf{I}$ , country is a net lender
- When  $\mathbf{S} < \mathbf{I}$ , country is a net borrower

The link between trade & cap. flows

$$NX = Y - (C + I + G)$$

*implies*

$$NX = (Y - C - G) - I$$

$$= S - I$$

*trade balance = net capital outflow*

Thus,

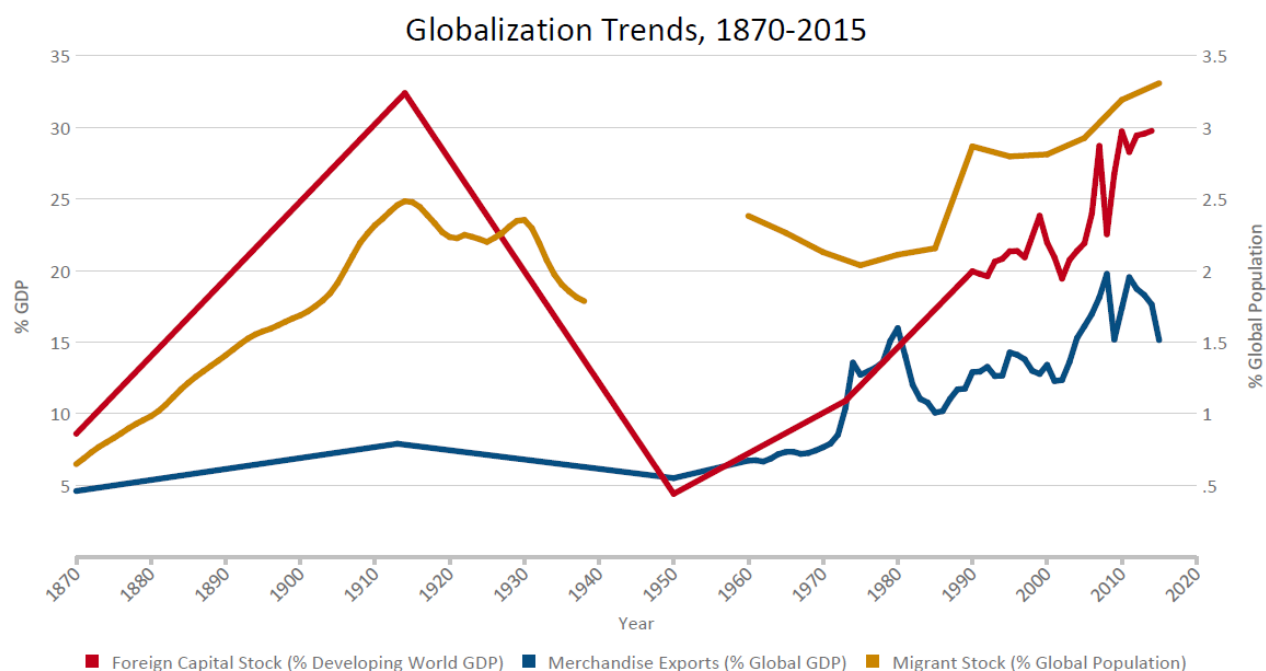
a country with a trade deficit ( $NX < 0$ )  
is a net borrower ( $S < I$ ).

## “The world’s largest debtor nation”

- U.S. has had large trade deficits, been a net borrower each year since the early 1980s.
- As of 12/31/2005:
  - U.S. residents owned \$10.0 trillion worth of foreign assets
  - Foreigners owned \$12.7 trillion worth of U.S. assets
  - U.S. net indebtedness to rest of the world: \$2.7 trillion--higher than any other country, hence U.S. is the “world’s largest debtor nation”

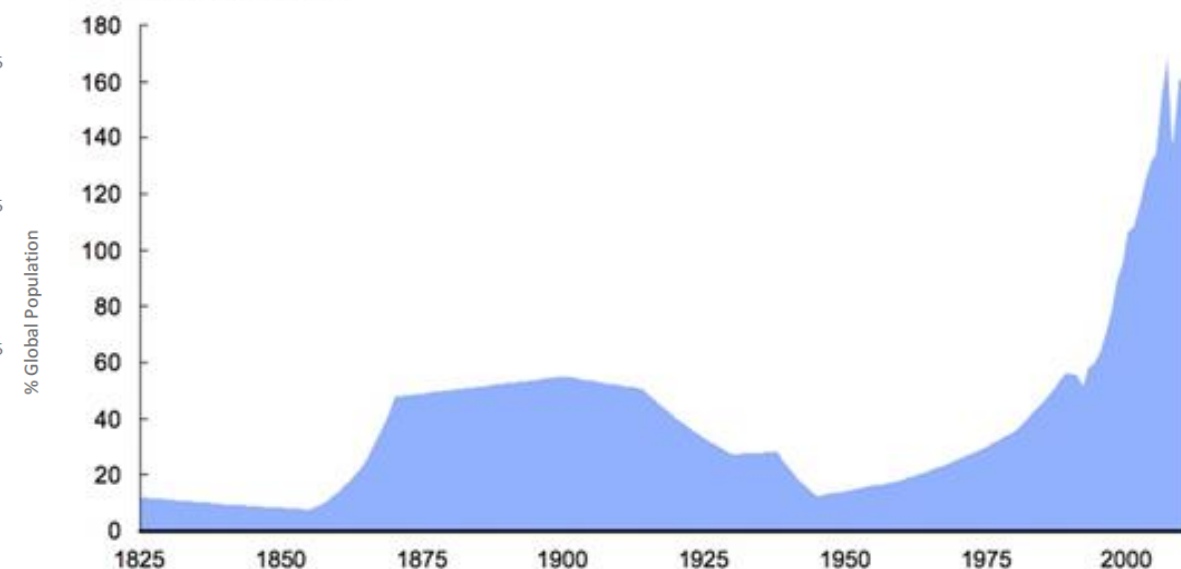


# Globalization I and II



## Two eras of financial globalization

Global foreign investment assets  
% country sample GDP<sup>1</sup>



<sup>1</sup> From 1825 to 1938, our country sample includes Canada, France, Germany, Japan, Netherlands, the United States, the United Kingdom, and other European countries. The sample expands as data becomes available. By 1990, the number of countries increases to 79.

SOURCE: IMF Balance of Payments; Federal Reserve Flow of Funds; US Treasury; Obstfeld and Taylor (2004); McKinsey Global Institute analysis



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# Globalization I and II

## Which is the most globalized era?

- **The *belle époque*, GI** (Gilpin 2001; O'Rourke, Williamson 1999); GII is just a return to a development trajectory inaugurated by the birth of the industrial age.
- **GII**, commodities and financial markets (Bordo et al. 1999), trade-to-GDP ratio (Findlay, O'Rourke 2007)
- **It depends** (Obstfeld, Taylor 2004): GI, for gross capital flows and stock of foreign capital; GII, flows of capital to the South and net capital flows

“By 1914, there was hardly a village or town anywhere on the globe whose prices were not influenced by distant foreign markets, whose infrastructure was not financed by foreign capital, whose engineering, manufacturing, and even business skills were not imported from abroad, or whose labour markets were not influenced by the absence of those who had emigrated or by the presence of strangers who had immigrated” (O'Rourke, Williamson 2001, 2).





# Globalization I and II

## Qualitative differences

- GII “more concentrated”, in Western countries and NICs (Newly-industrialized countries)
- Real-time world financial markets
- Breadth and depth of trade and financial cross-border activity;
- Speed of economic change
- Scale of gross economic flows of goods
- International division of labor
- Institutionalization of international economic relations
- Transnational enterprises
- The problem of governance...





# John Maynard Keynes: free trade evangelism

“Am I a Liberal?”, 1925 (*The Nation and Athenaeum*)

“There were always **two arguments** for Free Trade—the ***laissez-faire*** argument which appealed and still appeals to the Liberal individualists, and the **economic** argument based on the benefits which flow from each country's employing its resources where it has a comparative advantage. I no longer believe in the political philosophy which the Doctrine of Free Trade adorned. **I believe in Free Trade because, in the long run and in general, it is the only policy which is technically sound and intellectually tight**”.







# John Maynard Keynes: free trade evangelism

“National Self-Sufficiency”, 1933 (*The Yale Review*)

“I was brought up, like most Englishmen, to respect free trade not only as an **economic doctrine** which a rational and instructed person could not doubt, but almost as a part of the **moral law**. I regarded ordinary departures from it as being at the same time an imbecility and an outrage. I thought England's **unshakable** free trade convictions, maintained for nearly a hundred years, to be both the explanation **before man** and the justification **before Heaven** of her economic supremacy. As lately as 1923 I was writing that free trade was based on fundamental "**truths**" which, stated with their due qualifications, no one can dispute who is capable of understanding the meaning of the words“.



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# John Maynard Keynes: free trade evangelism

“National Self-Sufficiency”, 1933

**“What did the nineteenth-century free traders, who were among the most idealistic and disinterested of men, believe that they were accomplishing?**

They believed--and perhaps it is fair to put this first--that they were being perfectly sensible, that they alone of men were **clear-sighted**, and that the **policies which sought to interfere with the ideal international division of labor were always the offspring of ignorance out of self-interest.**

In the second place, they believed that they were solving the problem of **poverty**, and solving it for the world as a whole, by putting to their best uses, like a good housekeeper, the world's resources and abilities”.







# John Maynard Keynes: free trade evangelism

“National Self-Sufficiency”, 1933

“They believed, further, that they were serving, not merely the survival of the economically fittest, but the great cause of **liberty**, of **freedom** for **personal initiative** and individual **gift**, the cause of inventive **art** and the glorious **fertility** of the untrammelled mind against the forces of privilege and monopoly and obsolescence.

They believed, finally, that they were the friends and assurers of **peace** and international concord and economic **justice** between nations and the diffusers of the benefits of **progress**”.



ILLUSTRATION: JOHN IRVING EVANS GETTY IMAGES



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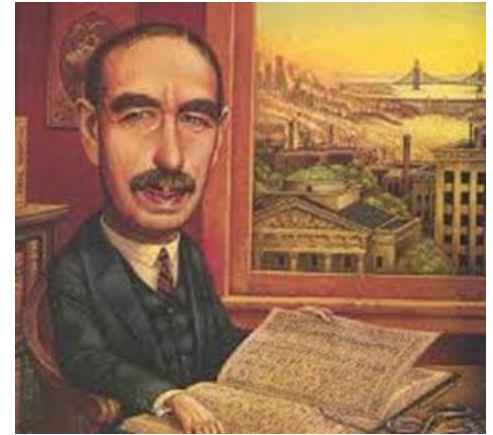




# John Maynard Keynes: national self-sufficiency

“National Self-Sufficiency”, 1933

I am **not** persuaded that the economic advantages of the **international division of labor** to-day are at all comparable with what they were ... A considerable degree of international specialization is necessary in a rational world in all cases where it is dictated by wide differences of climate, natural resources, native aptitudes, level of culture and density of population. But over an increasingly wide range of industrial products, and perhaps of agricultural products also, I have become doubtful whether the economic loss of national self-sufficiency is great enough to outweigh the other **advantages of gradually bringing the product and the consumer within the ambit of the same national, economic, and financial organization.**



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# John Maynard Keynes: national self-sufficiency

“National Self-Sufficiency”, 1933

Experience accumulates to prove that most modern processes of **mass production** can be performed in most countries and climates with almost equal efficiency. Moreover, with greater wealth, both primary and manufactured products play a smaller relative part in the national economy compared with houses, personal services, and local amenities, which are **not equally available for international exchange**; with the result that a moderate increase in the real cost of primary and manufactured products consequent on greater national self-sufficiency may cease to be of serious consequence when weighed in the balance against advantages of a different kind. **National self-sufficiency, in short, though it costs something, may be becoming a luxury which we can afford, if we happen to want it.**



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# John Maynard Keynes: national self-sufficiency

“National Self-Sufficiency”, 1933

“The decadent international but individualistic **capitalism**, in the hands of which we found ourselves after the war, **is not a success**. It is not intelligent, it is not beautiful, it is not just, it is not virtuous--and it doesn't deliver the goods”.

“We each have our own fancy. Not believing that we are saved already, we each should like to have a try at working out our own salvation. **We do not wish, therefore, to be at the mercy of world forces working out**, or trying to work out, some uniform equilibrium according to the ideal principles, if they can be called such, of laissez-faire capitalism. There are still those who cling to the old ideas, but in no country of the world to-day can they be reckoned as a serious force. **We wish--for the time at least and so long as the present transitional, experimental phase endures--to be our own masters, and to be as free as we can make ourselves from the interferences of the outside world.**

Thus, regarded from this point of view, the policy of an increased national self-sufficiency is to be considered, **not as an ideal in itself**, but as directed to the creation of an **environment** in which other ideals can be safely and conveniently pursued”.



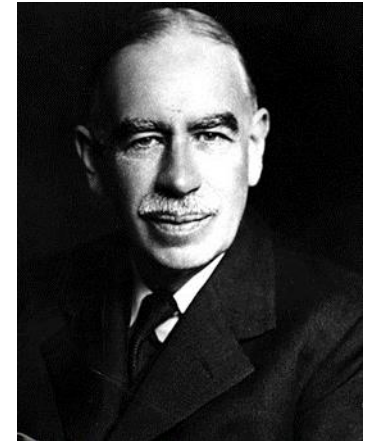


# John Maynard Keynes: national self-sufficiency

“National Self-Sufficiency”, 1933

“I sympathize, therefore, with those who would **minimize**, rather than with those who would maximize, **economic entanglement among nations**. Ideas, knowledge, science, hospitality, travel--these are the things which should of their nature be international. But let **goods be homespun** whenever it is reasonably and conveniently possible, and, above all, let **finance be primarily national**”.

“I am inclined to the belief that, after the transition is accomplished, a greater measure of national self-sufficiency and economic isolation among countries than existed in 1914 may tend to **serve the cause of peace**, rather than otherwise”.







# Seriously, man... *that* Keynes?



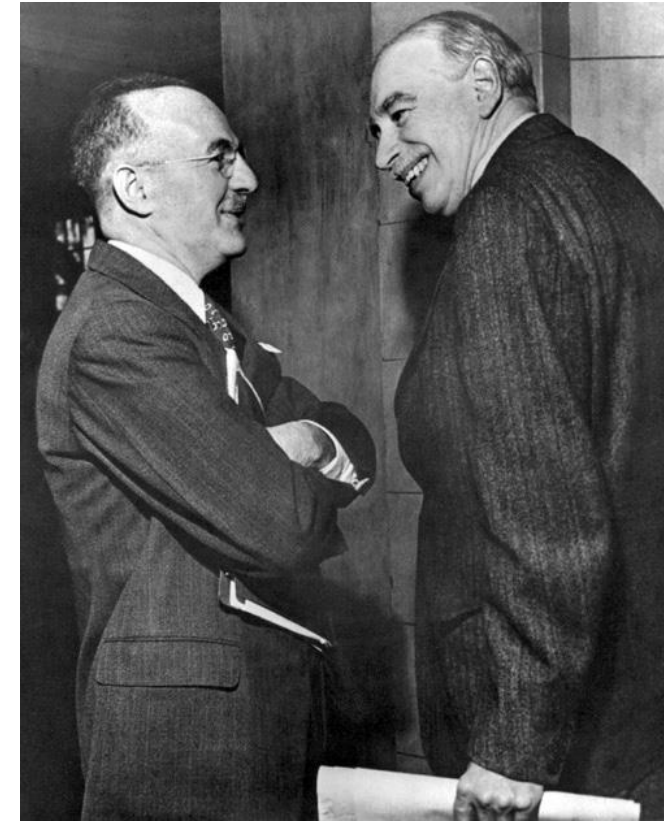
Anna Carabelli – Mario Cedrini  
**SECONDO KEYNES**

*Il disordine del neoliberismo  
e le speranze di una nuova Bretton Woods*

Pamphlet

This site in the town of Carroll, named "Bretton Woods" in 1905 to recall the original land grant of 1776, was chosen in July 1944 as the location of one of the most important meetings of the 20th century. Convened by the allied nations before the end of WWII and attended by representatives of 44 countries, the Bretton Woods Conference established regulations for the international monetary system following the war. The conference created the International Monetary Fund and the future World Bank, and linked the exchange rate of world currencies to the value of gold.

CASTELVECCHI



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# The importance of an international monetary system

## Monetary orders, monetary systems (Mundell 1972)

- Monetary **order**: set of institutions and arrangements governing money supply (*commodity* money, *fiat* money)
- Monetary **system**: *modus operandi* of the monetary order (mechanisms governing interactions between trading nations – money and credit instruments of national communities in foreign exchange, capital and commodity markets)



Es. Prewar gold standard and interwar gold standard: same “order”, different “systems”.

“As Joseph Nye has famously said about the security system, the monetary system is **like oxygen**: You never notice it until its absence poses serious, even existential, problems”  
(Bergsten 2014).





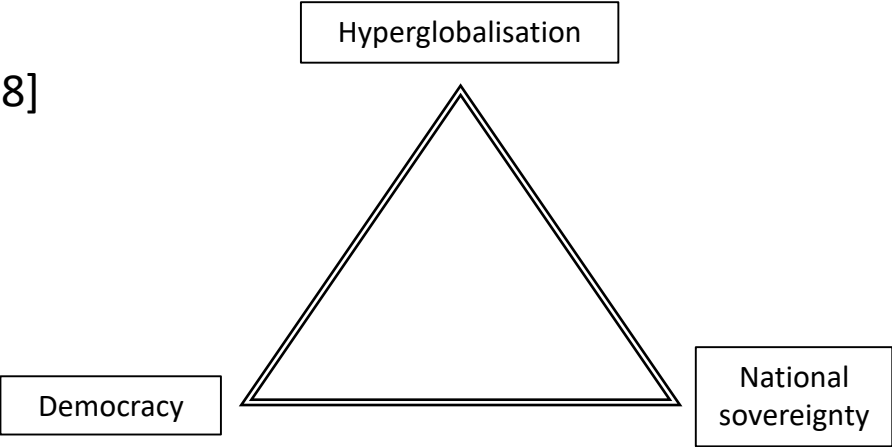
# The importance of an international monetary system

“**The main function** of the International Monetary System is to contribute towards global macroeconomic and financial **stability** by maintaining **stable exchange rates**, ensuring **sustainable current account** positions, providing an **adequate** amount of international **liquidity** and enabling **orderly adjustment** to external shocks” (UNCTAD *TDR* 2015, p. 55)

“Most countries have their own currencies; a means of exchanging these currencies is needed if business is to be conducted across national boundaries. The international monetary system establishes **the rules by which countries value and exchange their currencies**. It also provides a **mechanism for correcting imbalances** between a country’s international payments and its receipts. Further, the **cost of converting foreign money into a firm’s home currency** depends on the smooth functioning of the international monetary system” (Griffin & Pustay 2013).



Rodrik’s political trilemma [Source: Core Econ, *The Economy*, ch 18]



**If we have ...**

**then ...**

**and as a consequence ...**

