The New IMS Architecture and the Spirit of the Bretton Woods

Rossi, Giovanni

KU Leuven

2005

The New IMS Architecture and the Spirit of the Bretton Woods

Giovanni Rossi

Abstract

Globalization is producing in-depth changes in international monetary and financial relations. A new International Monetary System is emerging, which is strongly integrated on a global scale and dominated by private financial markets. In other words, as a consequence of this globalization process, the spirit of Bretton Woods has been forsaken. In this new IMS, emerging markets have become liberalization of capital account processes that have been hit by banking and monetary crises. Is this new instability era irreversible? Is it possible to go back to the Bretton Woods agreements, but to the spirit of Bretton Woods? What is the right way to move to it? Why is this trail so steep? This paper advances some propositions about the kind of institutional framework that can be used to stabilize the monetary and financial system. In the light of the recurrent monetary crises, the limits of the new architecture proposed by the IMF are stressed. We suggest another answer based on the rules of the world.

INTRODUCTION

With the disruption of the Bretton Woods order, the regulation of the international monetary system, hitherto provided by national and international public authorities, has been replaced by regulation based on freer functioning of the markets. This systemic transformation, at the heart of the process of financial globalization, has been accompanied by a change of attitude and doctrine of these authorities and, in particular, the International Monetary Fund (IMF). In the course of the 1980s, the Fund converted to an unconditional preference for liberalization and external openness of economies. His doctrine was thus in line with the new world monetary and financial order: the abandonment of the foundations of the Bretton Woods order found its completion with the abandonment of what had inspired this order.

The violence of the financial turmoil that affected emerging countries from the mid-nineties tempered this attitude and raised awareness of the urgent need to consolidate the architecture of the international monetary system (first section). An in-depth diagnosis of the characteristics and mechanisms of these new types of crises is obviously a prerequisite for designing therapies designed to strengthen the resilience of emerging economies to external shocks and to increase the stability of the financial system on a global scale. However, the first measures adopted over the past five years do not seem to us to be fully benefiting from these tumultuous years. The reforms contained in the new architecture of the international financial system, while necessary, may not be sufficient to effectively prevent or significantly reduce the effects of crises (Section II). Other more radical measures seem necessary (third section).

1. THE CRISIS OF THE 21ST CENTURY

Financial crises are not a new phenomenon, since during the last twenty years, 125 countries have faced this problem. However, the crises of the nineties in Southeast Asia and Latin America offer original features that distinguish them from past crises. In the first place, monetary crises are triggered in a brutal manner, without any possibility of predicting them, despite the progress that has been made in the development of early warning indicators. Second, the banking and monetary difficulties tend increasingly to appear simultaneously, expressing a strong interweaving of factors of fragility

Financial, and a change in the sequence of manifestations of crisis (before the nineties, banking difficulties appeared to be the culmination of other disorders, whereas they are now one of the first symptoms). Finally, the contagion of crises is of unprecedented magnitude. These three stylized facts characterize a change in the nature of the monetary crises of the nineties compared to previous decades. While the latter were largely driven by the current account - and thus by real imbalances - the recent crises are driven more by the capital account, highlighting the importance of financial factors and, in particular, the determining role of liquidity in current monetary and financial imbalances.

Faced with the challenge of these crises, the Fund's doctrine has undergone a new shift: the agenda is no longer unconditional, rapid and complete liberalization, but timely, gradual and orderly liberalization. The usual justification for this new attitude is based on asymmetries of information, a source of market failure. Information asymmetry indeed favors mimetic behavior on the part of investors, which can be a source of instability and violent market reversals. Recognition of these failures of market mechanisms militates in favor of public interventions. It also led the Fund to advocate openness management and preconditional liberalization as part of a controlled sequence of reforms aimed at strengthening the fundamentals of national economies.

To better understand the nature and characteristics of the crises of the nineties, it is necessary to examine more closely the set of determinants at the origin of these crises. Depending on whether exogenous influences or endogenous factors are favored in the economies concerned, two diagnoses can be made that lead to different therapeutic recommendations.

1.1 National crises, products of financial globalization

A first possible diagnosis consists in underlining the determining role of exogenous factors in the affected countries. In this perspective, the most frequently cited cause is the extreme volatility of international capital movements which, in contexts of international financial strains, are likely to withdraw indiscriminately from the emerging markets where they have been. placed, sometimes on the basis of mere rumors, as even the fundamentals of some of these countries are sound.

Private capital flows to emerging countries have been particularly volatile in recent years. They began to grow very rapidly in the early nineties, reaching in terms of grossed $213 billion in 1996, before collapsing to less than $ 60 billion in 1998. In net terms, the violence of reversals is also impressive. During the peso crisis, the reversal of capital flows between the peak of 1993 and 1995 accounted for 13% of Mexico's GDP. In 1997 alone, the five Asian countries hardest hit by the crisis experienced a reversal equivalent, on average, to more than 10% of their GDP.

If the crisis is mainly linked to causes exogenous to the affected economies, we understand that it is extremely difficult to predict the break-up. The fact that the usual warning indicators were in default during the Asian crisis, surprising all observers, argues in favor of this first diagnosis.

In addition, this interpretation implies that the extension of the crisis tends to operate essentially by a logic of pure contagion (Masson, 1998) or, in other words, according to mechanisms largely independent of the basic data of the economies contaminated. The extension of the crisis would therefore operate according to temporal and spatial sequences which, by definition, would also be difficult to predict. Correlatively, no country would be immune. The crisis would then assume a self-fulfilling character. Pan-European agents' behaviors, the flight to quality, the use of leverage, etc. can explain the greater contagiousness of recent crises.

Finally, the transmission to emerging countries of external shocks is frequently accompanied by an amplification of disturbances. This phenomenon has been theorized under the name monsoonal effect (monsoonal effect) by Masson (1998): a change, even a relatively minor one, occurring in the big industrial countries can provoke violent disturbances in the countries of the South when The economies of these countries are highly integrated with international financial markets. Capital flows to emerging markets are extremely sensitive to interest rate fluctuations in major global financial centers. This mechanism is indeed present both in the outbreak of the Mexican crisis (tension of US policy in 1994) and in the case of the Asian crisis (tension on long securities in Japan in 1997).

Another obvious source of monsoon effect comes from the volatility of exchange rates. Since the introduction of flexible exchange rates in the mid-1970s, the exchange rates of the major currencies - the dollar, the mark and the yen - have fluctuated widely in both nominal and real terms. Thus, between 1976 and the beginning of 1980 for the yen, and between the end of 1980 and the beginning of 1987 for the dollar, real exchange rates varied within a range of 40 to 60% (Isard and Faruqee, 1998). Since the early nineties, the yen has experienced a rise and fall of more than 30% in real terms. During the period 1994-97, the main exchange rate fluctuations concerned not the currencies of the Asian emerging economies but those of the G-3. However, the exceptional fluctuations of the yen against the dollar have exerted a destabilizing influence on the balances of payments of the Asian countries in crisis.

If crises are explained by pure contagion or if emerging economies are particularly exposed to external shocks, then financial openness can be considered, from the point of view of the contaminated country, as a major factor in the exposure to the risk of external shocks: it leads to a wider immersion of the entire national economy in the turbulence of the external environment. Therefore, the maintenance of exchange controls and restrictions on capital movements insulates the country and removes the risk of crisis. These measures may then be considered, in certain circumstances, as an effective strategy for crisis prevention.

1.2 Crises linked to the fragility of national economies

If, conversely, the crisis experienced by a country is interpreted mainly as the result of endogenous factors, what is at stake is not the behavior of lenders or creditors or foreign investors, but that of the domestic agents and the pre-existing fragility of the economies: excessive public deficit and indebtedness, deficiencies of the banking system, poor internal allocation of the external contributions, etc.

In the case of Asian crises, the fragility of national banking systems and the weakness of banking supervision have been decisive. In support of this thesis, we can note, for example, that the crisis has taken on aggravated forms (bank failures, depositors' panic and acute liquidity crisis) in countries where the fragility of the banking systems was most marked compared with countries with stronger banking structures (Chile, Brazil, Hong Kong, Taiwan).

If the crisis in a country is essentially endogenous, liberalization (internally and externally) cannot be held responsible for triggering it. Liberalization cannot be incriminated either in terms of the mechanisms of contamination to the extent that it operates by the fundamentals: the transmission of the crisis from one country to another is caused by the vulnerability of contaminated countries (insufficient foreign exchange reserves in the face of external commitments, overvalued currency, bank fragility, etc.). Like a domino effect, the contagion follows privileged lines that are fairly easy to predict.

1.3 Complex crises with embedded factors

Today, the interpretations of recent crises tend to be organized around two opposite patterns: either we consider that they reflect the existence of self-fulfilling and unpredictable financial panics in financial markets intrinsically unstable, justifying extreme caution in financial liberalization; either these crises are the result of previous vulnerabilities may be identified by the early warning signals that require corrective action by the authorities. We will recognize here the opposition between authors such as Wyplosz (1999) on the one hand, and Tornell (1999) on the other.

It seems to us that financial crises in emerging countries cannot be reduced, without impoverishment, to one or other of the terms of this alternative. In our opinion, these crises are neither exclusively endogenous nor exclusively exogenous. These two categories of factors are intimately combined. This, it seems to us, is one of the main lessons to be drawn from the experience of the years 1994-98: the financial turmoil is explained by the interweaving of these causes. It alone makes it possible to understand both the trigger mechanisms and the propagation mechanisms.

Correlatively, the usual distinction between crises related to fundamentals and self-fulfilling crises is probably less robust than it appears at first glance.

The explanation of crises by fundamentals (endogenous factors) has a limited scope, for certain episodes, when the explanation could only be given after the event. Indeed, any economy, whatever it is, always presents some zones of fragility. As a result, when a crisis occurs without it having been planned, the credibility of ex post reinterpretations is diminished. Subsequent explanations tend to resemble ad hoc rationalizations that shape or subordinate facts to the requirements of the theoretical framework of interpretation.

Conversely, it is true that any self-fulfilling crisis must be based on certain underlying vulnerabilities, but the elements that appear a posteriori as weaknesses were not understood as such prior to the crisis (this is why that the crisis can be described as self-reliant). These weaknesses, or were not perceived as being capable of crisis, or were not apparent a priori and were revealed by the crisis, particularly because it leads operators to reinterpret in a radically different way previously available information on the country's situation. Mutatis mutandis, the concept of a self-fulfilling crisis thus raises, in our view, an objection similar to that which the reverse interpretation calls for. External shocks destabilize an economy all the more surely because their impact is borne by the structural characteristics of the economies that suffer them. While the Asian emerging economies have suffered from the monsoon effect because of their high sensitivity to interest rate and foreign exchange rate fluctuations, it is largely because their currencies were strictly anchored to the dollar prior to the crisis.

From our point of view, the distinction between crises related to fundamentals and self-fulfilling crises is simplistic because, for each of these two pure forms, it is associated with the two extremes of the spectrum of possibilities:

- that of total unpredictability, in which the occurrence eventuality of the crisis is not an issue (which can even be imagined);

- that of perfect predictability where the relevant question is not whether and where the crisis will occur, but rather when it will occur.

However, pre-visibility is not binary. It is a question of degree. This is particularly true of the financial phenomena for which the mechanisms are largely determined by anticipations and the game on information that interconnects all actors of the financial markets on a global scale

2. THE NEW ARCHITECTURE IN QUESTION

Reflecting on the nature of recent financial crises is not an abstract speculation. The appropriate therapy must be based on the diagnosis of the roots of the disease to be treated. The preceding reflections can thus help to appreciate the interest and the limits of the reforms that have been initiated since the mid-nineties.

These reforms have two components: first, to try to prevent the outbreak (and spread) of crises and, secondly, to reduce the consequences.

2.1 The main features of the new architecture

The curative action is quite traditional. It consists of expanding the financial resources that can be mobilized to help countries in difficulty. Five major initiatives have been taken in this regard in recent years:

- the creation of an emergency financing mechanism, which is more flexible and faster than traditional financing (in 1994);

- the conclusion of the New Borrowing Agreements (NAE), designed on a larger scale, following the model of the General Loan Agreements (GATS) of the 1960s;

- the increase of 45% of the quotas (their total amount is increased to 288 billion dollars);

- the creation of a special SDR allocation of SDR 21.4 billion, doubling the amounts already allocated to member countries;

In the same vein, Jeanne (1997) considers that apart from the possibility of fundamentals being very favorable, or frankly unfavorable, there would exist a critical zone characterized by multiple equilibria. In this intermediate zone, an eventual speculative attack is self-fulfilling in that it results from a change in the behavior of the operators and not from a sudden modification of the fundamentals (transition from an optimistic equilibrium to a pessimistic equilibrium). However, the attack is not random, since it results from an earlier fragility of the economy, that is to say its entry into the risk zone, induced by the degradation of its fundamentals.

- the creation (in December 1997) of a new Emergency Financing Facility: the Supplementary Reserve Facility, which was first used in January 1998 for South Korea.

The broadening of the range of financing instruments aims not only to increase the Fund's intervention capacity, but also and above all to increase its speed of intervention. The introduction of the Prevention Credit Line (LCP) in April 1999 is a new step in the IMF's commitment. Indeed, with the LCP, the IMF strives to combine curative measures, prevention and action on incentives (reduction of moral hazard). The LCP consists of a possibility of access to additional financial resources that are a priori uncapped (but probably of the order of 300 to 500% of the quota). It is made available to countries that respect conditions of good conduct and good management (with the possibility of dequalification each year). It is intended not to remedy actual difficulties, but to provide the fundamentally sound economies with a deterrent against the risk of contagion. It is above all a means of building preconditionality and consolidating the Fund's power vis-à-vis the Member States.

The essential originality of reforms for the construction of a new financial architecture therefore focuses on preventive measures. The agenda for these reforms is in one word: transparency.

The prevention of financial crises involves improving the agents' information on the state's situation, thus increasing the transparency of the markets. By informing operators about the macroeconomic situation of countries, particularly with the aid of leading indicators, the authorities are trying to contain the highly destabilizing effects of overexcitation. The early warning system is based on a battery of indicators such as the state of foreign exchange reserves, the evolution of the balance of payments, the level of the budget deficit, inflation and domestic interest rates. It is intended to detect in advance the risk of crisis and thus prevent the appearance or, at least, to reduce its severity by avoiding the accumulation of imbalances.

In April 1996, a more general and systematic information dissemination scheme, the Special Data Dissemination Standard (SDDS), was established, which organizes, on a voluntary basis, the collection and dissemination of data on key economic policy variables, the monetary and financial situation of the member countries. This first reform orientation was completed and reinforced by the creation of the General Data Dissemination Standard (set of standards for the collection and dissemination of information applicable to all member countries), which came into operation in May 2000.

This search for Transparency is based on the belief that a broad dissemination of higher quality information will ensure greater stability, allowing market discipline to operate more effectively and streamlining the formation of international investor expectations. . Increasing the reliability and homogenizing the sets of information available to agents, it is also to avoid adverse effects resulting from information asymmetries. As a result, the IMF strives to be a stakeholder in the information games that characterize the functioning of globalized financial markets. Incidentally, by extending transparency to the functioning of the banking sector, especially in developing and emerging countries, the Fund is also expanding its sphere of competence.

Indeed, even though bank supervision is the sole responsibility of the competent national authority, the IMF's mission now goes beyond monitoring only the macroeconomic policies of governments. It also gradually extends to monitoring compliance with prudential standards and detecting fragility factors in national banking systems. Correlatively, the Fund's conditionality, which was initially purely macroeconomic, changed in the 1980s to include choices about the structures of economies. In the nineties, this conditioning was extended and deepened to the microeconomic level, now including the restructuring of banking systems and the dismemberment of large groups.

2.2 Its limits

The expression new architecture is both practical and ambiguous. It is practical because it offers a neutral and accommodating semantic substitute for what seems today out of reach: a real reconstruction of the international monetary system. However, it is ambiguous because it suggests what it is obviously not: a profound modification of the supporting elements and the framework of the building considered in its entirety. Far from attempting to thwart or alter the forces underlying the transformations of monetary and financial relations on a global scale, national and international public authorities are rather conforming to the maxim of realism "if you can" Do not beat them, join them. They are confined to accompanying global financial liberalization through piecemeal adaptation measures, for want of being able to push for more radical reforms. The preference generally asserted today by the majority of experts for incremental (or modest) rather than radical (or ambitious) measures is a good reflection of this attitude.

The adaptive nature of the changes made (or advocated) is not in itself a limit. It is rather a choice. However, the very foundations of this one, even more than its technical modalities, seem to us to be discussed.

2.2.1 Transparency: a solution that poses problems

In the first place, the systematic search for transparency is based on the assumption that all is always good to say. If markets are able to integrate fully all publicly available information (semi-strong informational efficiency), while transparency is beneficial: it reduces the volatility of the exchange because information (enriched through transparency, for example on the actual or potential fragility of a country) is integrated in advance in prices. The concretisation of this fragility will have no effect on price, thus avoiding the phenomena of over-reaction that may result from truncated information contexts. The relevance of this hypothesis efficiency is however not empirically assured and there is no guarantee that the systematic dissemination of information prevents the occurrence of crises or reduce the magnitude.

The limits of the search for transparency also appear at the level of the alert device. Our knowledge of the mechanisms of financial crises is too rudimentary for us to be able to develop a reliable battery of advanced crisis indicators. Correlatively, an early warning device has two risks of failure: either to remain silent or to trigger alarms incorrectly.

But it is even more serious: in a world where there is a plurality of equilibriums with the possibility of discontinuous passages from one to the other, it cannot be excluded that the triggering of crisis warning signals may cause a loss brutal investor confidence, capital outflows and then panic movements. This ambivalence of information and the risks associated with its diffusion have been perceived by the IMF, whose progress in transparency is taking place at a slow pace. Rather than publish systematically the information available to it or the opinions it issues as part of its surveillance activity, the Fund makes this dissemination subject to the agreement of the member countries, by encouraging them to consent to it. This relative prudence is explained by the Fund's concern not to precipitate disorder and not to compromise the quality of the negotiations with the Member States. On the other hand, it is plausible that the systematic non-disclosure of information on the situation of Member States reduces the effectiveness of the Fund's supervision (its ability to put pressure on governments). In short, even if the Fund had - which is far from the case - a good ability to predict crises, it could not predict them (publicize the information in advance) without risk perverse effects. At least for this reason, transparency does not seem to us to be a sufficient condition for market stability.

2.2.2 An incorrect presumption of responsibility

The SMI's new architecture projects express a significant change in the public authorities' attitude towards anti-crisis therapy, which is associated with a de facto reversal of the diagnosis of the origin of the crises.

In the course of the 1980s, attempts to remedy financial instability were mainly based on the search for better coordination between the main industrial countries (especially in the G -7). Today, this orientation is largely absent from attempts to prevent financial turmoil: it has given way to surveillance of emerging economies, which are expected to join the good housekeeping club. The implicit postulate underlying this new attitude is that financial instability would find its source exclusively in these economies.

Now, the characterization of recent crises (supra, part one) shows to what extent this implicit presumption of responsibility is excessively reductive, and in some cases incorrect.

The confrontation of the dysfunctions to be remedied and the solutions adopted for this purpose clearly show the limits of the therapies applied. From our point of view, these are not ineffective. Open yards for the construction of the new architecture are undoubtedly advancements in the quest for greater stability.

However, no real architectural reform will be possible as long as more radical changes are not simultaneously adopted to reduce the instability of both international capital flows and the exchange rates of major currencies.

3. DEFINING A NEW PRINCIPLE OF INTERNATIONAL MONETARY ORGANIZATION

From the point of view of state governance, international financial integration has two main implications. In the first place, this process brings to an extreme the exacerbation of tensions between increasingly integrated economic systems and fragmented political systems. Monetary and financial instability is partly due to the fact that markets are benefiting from the difficulty faced by national authorities and international institutions in setting new rules of the game on a global scale.

Secondly, the contagion associated with the financial crises of the nineties shows the importance of the externalities - here negative - generated by financial integration. On the one hand, the interconnection of markets has increased as a result of financial liberalization, leading to an interlocking of factors of fragility. On the other hand, the economic policy strategies adopted by countries with significant financial openness affect not only neighboring countries (regional contagion), but sometimes also world markets.

International financial integration thus directly raises the question of its governance at its level.

Financial globalization - by accentuating global interdependencies - puts international institutions and states in a dilemma. On the one hand, increasing integration calls a need rules substantive that is to say rules precisely defining each state standards of conduct in its relations with other states. On the other hand, however, the increase in international capital flows limits the authorities' room for maneuver. It restricts states' ability to enforce these rules and that of international organizations to enforce them. The substantive rules then tend to be superseded by procedural rules which do not define behavioral norms a priori, but are based on the definition of non-imperative guiding principles common to the Member States and intended to guide their strategies. Procedural rules also aim to bring the behavior of states and private agents closer together, thereby reinforcing their compatibility.

A particularly important procedural rule for the new architecture concerns international capital movements as part of a revision of the Bretton Woods Agreements (Section 3.1). However, procedural rules alone do not seem to be able to ensure the stability of the globalized monetary and financial system. Thus, as recalled by the Asian crisis in 1997, the large exchange rate fluctuations between the major currencies produce powerful negative systemic effects on the world economy. Therefore, a key substantive rule is the establishment of a target area between the dollar, the euro and the yen (section 3.2) as in Kirrane (1995).

3.1 The integration of international capital flows into the Bretton Woods Agreements

The financial crises of the 1990s show that emerging economies have lower financial regulatory capabilities than developed economies (Stiglitz), 1998). They are therefore particularly vulnerable to shocks after the financial opening. Such a finding argues for a cautious approach to liberalization.

For some - among others Kirrane (1995), McKinnon and PiIl (1998); Eichengreen (1999) - Controls on international capital movements could offset temporary institutional inadequacies in emerging countries. More specifically, measures of the type adopted by Chile as early as June 1991 would have the advantage of reducing the vulnerability of the financial system to external shocks while allowing the authorities to undertake structural reforms with long-term effects. Compared to other possible control systems, the Chilean capital inflow tax - in the form of a one-year unpaid mandatory deposit with the central bank - has two main advantages: on the one hand it is a system based on the mechanisms of the

This is because the implicit rate of the tax changes with interest rates and, on the other hand, it further penalizes short-term capital inflows, which must reduce the vulnerability of the market. facing the sudden reversal of investor sentiment. Control responds to the institutional transition between a repressed financial system and a liberalized financial system. Indeed, permanent controls lose their effectiveness over time (Allegret, 2000).

However, it must be taken into account that international financial integration can lead to the emergence of centripetal forces. If developing countries consider that gains related to financial openness outweigh costs and that it is essential to integrate into international financing markets as quickly as possible to maximize these gains, then they may be tempted to accelerate financial liberalization even if they are not ready. Given the negative externalities of financial integration, such a strategy can be destabilizing for the international financial system. At the same time, the use of controls can be interpreted by investors as a challenge to the financial liberalization strategy. Such a negative signal is then likely to cause a massive capital flight and / or lead to an increase in the cost of borrowing on the international capital markets for the country in question.

In total, centripetal forces and a negative signal may limit the incentive for emerging countries to resort to capital controls as a means of integration into international finance. The controls will then be used more as a strategy of "preservation of the market" (Cohen, 2000) that as a market protection strategy (or promotion of reforms) in the sense that the objective is to stabilize the international financial system.

In this perspective, it is the controls on exits that will be favored in crisis situations, as in the case of Thailand (1997) and Malaysia (1998). On controls as a strategy to promote reforms, see Allegret and Dulbecco (2000).

Statement of the Interim Committee on the Liberalization of Capital Movements under an Amendment of the Article. Capital considerations to the "individual circumstances of countries, in order to maximize the chances of success, not only for each country, but also for the international monetary system".

As the IMF press release suggests, it is possible to go beyond a simple code of conduct by integrating the issue of international capital flows into the mandate of the Bretton Woods institution. To this end, an amendment to its statutes is necessary.

A first way of looking at things is to reason by analogy with the convertibility of the current account (Fischer, 1997). More specifically, in the same way that Article VIII of the Bretton Woods Agreements establishes the convergence of the current account as a rule and that Article XIV specifies the transitional measures, the amendment related to the convertibility of the capital account allow a stable insertion, that is to say, institutionalize a sequentiality in the financial openness of countries. However, the current account-capital account analogy is misleading. Indeed, if the convertibility of the current account refers to payments linked to the movement of goods and services - the liberalization of the latter being left to other institutions such as the World Trade Organization - the convertibility of the capital account carries directly on capital movements which certain segments are beyond the competence competent and jurisdiction of the IMF.

Therefore, a second way of proceeding is to create a specific article related not only to the convertibility of the capital account, but also to the freedom of international capital movements. The presence of centripetal forces and the negative signal effect also call for an explicit reference to the possibility of using controls on international capital movements. The IMF should thus specify the conditions for their use by the precise statement of principles and guides around three main questions concerning (Cohen, 2000): (i) the types of restrictions allowed, which implies an evaluation of the various systems adopted by developing countries; (ii) the circumstances in which the authorities may impose a control; (iii) the procedures to be implemented. The principles and guidelines set out by the IMF would be negotiated multilaterally with the Member States, each then free to use them after consultation with the IMF.

One of the issues is whether to allow only controls on Chilean-type entries, or whether to take into account exit-type curative controls as adopted by Malaysia. While the former are favored by international institutions because of their flexibility and their link with market conditions, the latter has had - accompanied by important reforms - a degree of efficiency to enable Malaysia to stabilize its economy after September 1998. In contrast, the preventive exit controls, ie before the onset of the crisis, as in Thailand, seem less effective. See Allegret (2000).

This event, still in the state of negotiations between Member States, is the subject of controversy since it may appear as a way to force the political authorities to liberalize their economies. However, it seems to us that such an initiative has the essential virtue of stabilizing the relations between the different actors of the financial markets around common standards. Thus, far from signaling the advent of a global economy without control, the assertion of IMF accountability for capital account convertibility and international capital flows would have the advantage of setting a clear framework of reference for the use of controls and the orientation towards liberalized financial systems.

3.2 Target areas as a substantive rule of the new architecture

In the face of exchange rate instability, corner solutions - flexible exchange rates or perfectly fixed rates (monetary union or currency board) - are nowadays widely recommended (Eichengreen, 1999). Others (Kirrane, 2003) propose strategies for regional anchoring of small currencies.

Another approach is to consider that the exchange rate stability of the G-3 countries can be considered as an international public good. Therefore, a key substantive rule is the establishment of a target area between the dollar, the euro and the yen.

Such a substantive rule implies breaking with the behaviors observed since the mid-eighties. Since that time, cooperation within the G-7 has been episodic and has occurred most often late, ie. after a long process of misalignment (Volcker 1995, Bergsten 1998). Such behavior is all the more likely if the authorities are unwilling to declare explicit bands, refusing to guide the market on the fundamental value of currencies and thereby promoting speculative phenomena.

The area must be declared publicly and form the subject of an institutional arrangement to defend it. Following the proposal of Bergsten (1998), the envisaged area could be +/- 15% around a central rate. This should be determined by States in close collaboration with the IMF to integrate this determination into a macroeconomic framework that takes into account both the balances of the three G-3 economies and the perspectives of the global economy. The width of the band must be large enough to allow periodic adjustments of the central rate without causing a discreet exchange rate change favorable to speculation. In order to take into account the independence of central banks - often in charge of implementing exchange rate policy - an institutional arrangement is needed. The organization of relations between central banks and finance ministers could be as follows:

- the G-3 finance ministers have co-responsibility with the IMF to develop the architecture of the exchange rate regime, namely (i) central rates; (ii) the width of the strip; (iii) the commitment to defend the target area. Ministers are also responsible for deciding, after consultation with the IMF and authorization by the IMF, changes affecting the exchange rate regime (new central rates or changes in the number of participating currencies, for example). At this stage of the implementation of the exchange agreement, central banks are present only to inform political decisions;

- central banks exercise full and independent control over the implementation of the target area. This means that they decide in a discretionary way about their intervention strategy and can set up reciprocal credit lines;

- when the economic policies underlying the maintenance of the target area conflict with the objective of price stability, negotiations between central bankers and finance ministers must be undertaken under the aegis of the IMF. In particular, central banks can take the initiative to obtain a revision of the target area;

- close consultations between central banks and ministries of finance should be organized through the IMF.

The creation of a target zone between the dollar, the euro and the yen is part of a double context from the point of view of the world economy.

On the one hand, since the beginning of the 1990s, there has been a worsening of external payments imbalances between the United States, Japan and the euro zone. The continuing widening of current US imbalances is due to a number of factors, including the growth gap vis-à-vis Japan and the euro area.

However, as in the first half of the 1980s, there is a coincidence between the worsening of these deficits and the appreciation in real terms of the dollar vis-à-vis the yen and the euro. In this perspective, the reduction of current account imbalances between the three areas seems to call for an adjustment of exchange rates towards more consistent with basic levels.

Specifically, it is about limit the extent of over-reaction phenomena that often accompany the exchange rate adjustment phases. However, given the considerable increase in US external liabilities and their net external debt position, any increase in the volatility of the euro-dollar exchange rate could be accompanied by an increase in US long-term interest rate via the dollar risk premium mechanism, which would certainly affect global interest rates and financing conditions in emerging economies.

Moreover, by guiding the markets on the exchange rate, approaches in terms of the microstructure of the foreign exchange market suggest that the probability of the occurrence of destabilizing behavior is reduced. Thus, large international capital movements linked to uncertainty about exchange rates are expected to narrow. The corollary is the possibility of a more stable integration of emerging economies into international finance. See Kirrane (2003).

Finally, the target area can be interpreted as a substitute for the coordination of economic policies within the G-3. Indeed, a target area - even as flexible as the one proposed here - implies a specific policy-mix. More precisely, to the extent that monetary policy is mobilized for the external objective - the manipulation of interest rates affects the exchange rate - it is up to fiscal policy to ensure the achievement of internal equilibrium. . Budget authorities must therefore have leeway in order to be able to act on the stabilization of the economy. In the absence of such margins, the feasibility of the target area is difficult to envisage: the full weight of the adjustment, ie in terms of internal and external objectives, is based on monetary policy. From this point of view, an exchange rate target within a target area is likely to contribute to the gradual decrease of divergences for sales budget

CONCLUSION

The considerable increase in international capital flows, the emergence of new markets and players have highlighted the need to tackle international monetary and financial problems in a radically renewed way. Discussions of global regulatory powers become central to the stability of the globalized monetary and financial system.

This article has highlighted the new types of rules to be mobilized in this new context. These relate, on the one hand, to international capital movements and, on the other hand, to the establishment of a target area within the G-3. They undoubtedly call for a strengthening of the powers and legitimacy of the Bretton Woods institutions.

Whichever path is chosen in this direction, one of the major challenges of the international monetary organization of the 21st century will undoubtedly be to find ways to make the expression of a certain national sovereignty and the unification of finance that transcends these sovereignties and makes regulation on its own scale necessary.

References

ALLEGRET, JP (1997), International Monetary Economics, Hachette Superior, Paris.

ALLEGRET, JP (2000), "What role for controls of international capital movements in the new architecture of the international financial system? ", International Economy, No. 81, 1st quarter: 77-108.

ALLEGRET, JP and P. DULBECCO (2000), "Global Governance versus Domestic Governance: What Roles of International Institutions? Communication to the Global Economics Transformation Conference after the Asian Economic Crisis, The Chinese University of Hong Kong, Peking University and World Economy, Hong Kong, May 26-28.

BÉNASSY-QUÉRÉ, A. and B. CŒURÉ (2000), "The future of" small "currencies, regional solutions versus wedge solutions", Revue d'Economie Politique, vol. 110, No. 3: 345-376.

BERGSTEN, CF. (1998), "How to Target Exchange Rates," Financial Times, November 20.

BERGSTEN, CF. (1999), "The Decline of the Dollar", World Economy Forum, Davos, January.

BERGSTEN, CF. and CR. HENNING (1997), Global Economics Leadership and the Group of Seven, Institute for International Economics, Washington, DC.

COHEN, B. (2000), "Taming the Pheonix: Monetary Governance After the Crisis," in G.NOBLE and J. RAVENHILL (eds), The Asian Financial Crisis and the Architecture of Global Finance, Cambridge University Press, forthcoming.

EICHENGREEN, B. (1999), Toward a new International Financial Architecture, a Practical Post-Asia Agenda, Institute for International Economics, Washington,

DC FISCHER, S. (1997), "Capital-Account Liberalization and the Role of the IMF", IMF Seminar: Asia and the IMF, September. INTERNATIONAL MONETARY FUND (2000),

IMF Staff Country Report, No. 00/46, March. INTERNATIONAL MONETARY FUND (2000),Washington, DC, ISARD, P. and H. FARUQEE (eds.) (1998), Exchange Rate Assessment, Extensions of the Macroeconomic Balance Approach, Occasional Paper, No. 167, IMF.

JEANNE, O. (1997), "Are Currency Crises Self-Fulfilling? A Test, "Journal of *International Economics, vol. 43: 263-286.*

KAHLER, M. (1995), International Institutions and the Political Economy of Integration, Brookings Institution, Washington, DC. MASSON, P. (1998), "Contagion: Monsoonal Effects, Spillovers, and Jumps Between Multiple Equilibria," IMF Working Paper, WP / 98/142, September.

KIRRANE, C. (1995). The Bretton Woods Experience and ERM. *European Economic Integration Review*, Vol. 13, p.23-34.

KIRRANE, C. (2003). The IMS and the Euro. *European Political Economy Review No. 1 (March 2003), pp. 153-65*

MCKINNON, RI and H. PILL (1998), "The Overborrowing Syndrome: Are East Asian Economies Different? In R. GLICK (ed.), Managing Capital Flows and Exchange Rates, Perspectives from the Pacific Basin, Cambridge University Press, p. 322-355.

POLAK, JJ. (1998), "The Articles of Agreement of the IMF and the Liberalization of Capital Movements," in S. Fischer (eds.), Should the IMF Pursue Capital-Account Convertibility?, Essays in International Finance, No. 207, May, p. 47-54.

RODRIK, D. and A. VELASCO (1999), Short-Term Capital Flows, Mimeo, May.

SANDRETTO, R. (1993), The power of money. Reflections on the crisis and the future of the international monetary system, Economica, Paris.

STIGLITZ, J. (1998), "More Instruments And Broader Goals: Moving Towards The Post-Washington Consensus," The 1998 WIDER Annual Lecture, Helsinki, January.

TORNELL, A. (1999), "Common Fundamentals in the Tequila and Asian Crises,"

NBER Working Paper, No. 7,139, May. VOLKER, RA. (1995), "The Quest for Exchange Rate Stability: Realistic or Quixotic? Speech delivered in the Senate, London University, November 29.

WYPLOSZ, C. (1999), « International Financial Stability », in KAUL I, I. GRUNBERG *et MA STERN (éds), Global Public Goods, International Coopération in the 21st century* Oxford University Press, New York, p. 152-189.