Fifth Lecture
Taming the Beast: Global Money and Finance

In what way is global money a “beast” and why does it need to be “tamed”?

The “Beast”: money and conflict

Money
• Means of exchange
• Store of value
• Unit of account
• Means of deferred payment

What makes money money?
• Non perishable
• Easily divisible
• Liquid

Acceptance
• Gold and labour time
• Symbolic money and the structure of authority and power

Public-Private tension
• Money = Quantity * Price
• Causality: from prices to money, from money to prices, or both?
• Money and prices: which is the “public,” which is the “private”?
• Capital and state

Global money
• More currencies, further complications
• State ⇔ Private
• State ⇔ State
• Domestic private ⇔ Foreign states
• Money and GPE

Balance of payment
• Production and uses
• Current account and the internal balance
• Saving balance and budget balance
• Capital account
• The balance of payments

How does the balance of payment balance?
• Direct adjustment
• Indirect devaluation/revaluation

Monetary order:
• Who rules?
• How?
• Why?
Features:
- Monetary stability and sovereignty: an oxymoron?

Monetary orders:
- Automatic
- Supernational
- Hegemonic
- Negotiated

Bretton Woods
- Free trade
- Regulated capital account
- Stable exchange rates

Adjustment: IMF and World Bank

Fundamentals: the Cold War
- Truman Doctrine
- Marshall Plan
- The “dollar shortage deal”: supply and demand sides
- Flooding the world with dollars

The reckoning
- Overvaluation
- Challenges to the US

August 1971: The end of Bretton Woods
- US domestic expansion
- Third world politics and global instability
- Conflict inflation
- Capital movement

Bretton Woods: An aberration?
- Capital movement
- Trade
- TNCs
- State vs capital

A new crisis?
Consumers Prices in the U.K. (1820=100)

Price increase from 1900 to 2000: **4.867%**

Price increase from 1300 to 1900: **769%**

THE BALANCE OF PAYMENT AND THE DOMESTIC ECONOMY

Production
(1) … Gross Domestic Product = Consumption + Investment + Government + (Export–Import)
GDP = C + I + G + (X – M)

Uses
(2) … Gross Domestic Product = Consumption + Saving + Taxes
GDP = C + S + T

Combining production and uses
(3) … C + I + G + (X – M) = GDP = C + S + T
(4) … I + G + (X – M) = S + T

Current account and the internal balance
(5) … (X – M) = (S – I) + (T – G)
Current Account = Saving Balance + Budget Balance
CA = SB + BB

Current account under barter
(6) … Current account = 0
X – M = 0

Current account under a monetary system
(7) … Current account = Change in Reserves
X – M = ΔRes

Current account under a credit system (+ve/–ve values denote fx inflow/outflow)
(8) … Current Account + Capital Account = Change in Reserves
(X – M) + CF = ΔRes

Ex. 1 $100 bn + (–$120 bn) = ΔRes  ΔRes = –$20 bn
Ex. 2 $200 bn + CF = –$10 bn  CF = –$210 bn
Ex. 3 (X – M) + $80 bn = (–$30 bn)  (X – M) = –$110 bn

Policy implications
In equation 8, substitute (SB + BB) for (X – M):
(9) … (SB + BB) + CF = ΔRes
(10) … (SB + BB) – ΔRes = –CF
Question 1:
The country has $100 bn in reserves, the saving balance \((SB)\) is \(-80 \text{ bn}\), the budget balance \((BB)\) is \(-20 \text{ bn}\), and there is no capital flow \((CF = 0)\). Can this situation continue indefinitely?

Question 2:
The current account is \(-100 \text{ bn} \) \((SB + BB = -100 \text{ bn})\), the capital account is an inflow of 100 \text{ bn} \((so \ -CF = -100 \text{ bn})\), and the country has no reserves. If capital inflow falls to 80 \text{ bn}, what must happen to \text{SB, BB or the currency?}
Brazil: Trade and Capital Flow ($mn)

NOTE: Monthly data expressed as 12-month moving averages.
"Real Liquidity" Index for the Industrialised Countries

* Computed as a ratio of "real" reserves to industrial production. "Real" reserves are given by foreign reserves minus gold expressed in SDRs, converted to US$ and deflated by the US CPI.

U.S. Dollar Reserves and Gold

Cash Reserves ($bn, right)

Gold Reserves ($bn, right)

Gold / Cash (%, left)

United States: Trade and the Dollar

GERMANY RELATIVE TO THE US: EXCHANGE RATES AND INTEREST RATES

NOTE: data are expressed as 12-month moving averages; SOURCE: IMF

UK RELATIVE TO THE US: EXCHANGE RATES AND INTEREST RATES

NOTE: data are expressed as 12-month moving averages; SOURCE: IMF

JAPAN RELATIVE TO THE US: EXCHANGE RATES AND INTEREST RATES

NOTE: data are expressed as 12-month moving averages; SOURCE: IMF
Credit to the Private Sector (% of GDP)

SOURCE: World Development Indicators