Regulation or Barbarism

The Case for National Economic Sovereignty

by Nicola Bullard

IN 1996, $97 BILLION OF PRIVATE CAPITAL flooded into Thailand, Indonesia, the Philippines, Malaysia and South Korea — the five countries most effected by the Asian crisis. In 1997, the tide had turned, and these countries experienced an outflow of $12 billion. In net terms, that is an astounding $109 billion reversal of fortunes.

In contrast, the United Nations Commission on Trade and Development's latest Trade and Development Report notes that there has been virtually no change in levels of foreign direct investment in these same five economies from 1996 to 1997. The lesson is very simple, and is now gaining wide acceptance amongst the economic establishment, the G7, and even the International Monetary Fund (IMF) itself: uncontrolled speculative capital was one of the major factors in the Asian economic collapse, and is a threat to the stability of the national economies and to people and their livelihood.

The responses to this revelation are varied: Malaysia's Prime Minister Dr. Mohamed Mahathir has taken matters into his own hands and implemented a series of tough capital controls, currency speculator George Soros — who lost a cool $2 billion in Russia — is calling for regulation, and even the IMF in a recent capital markets report notes that "the combination of a weak banking system and an open capital account was an accident waiting to happen." Having made this Edison-like discovery, the Fund continues that "policymakers need to undertake an orderly opening of their financial systems and may need to consider imposing temporary measures to restrain certain types of inflows."

Welcome to the real world.

That we need to cool down hot money is evident. How to do that is the more difficult question. The answer depends on how you perceive the problem.

Free market economists see it as a problem of safety nets and information; they say we need a better system of checks and balances to readjust the inefficiencies of the market and more information so that the market can make better decisions. The kind of regulatory mechanisms proposed aim to improve prudential supervision and transparency, make sure institutions behave predictably, establish global norms which clear the stones from the path of the free market and put up bold signposts. In other words, they want to reduce market risks.

Others, however, see the problem differently. It is not a matter of making the market work better for capital, but making the market work better for people. Regulation of speculative capital flows is the first and necessary step so that people and governments can reclaim their economic sovereignty, rather than being swept aside by the tide of private capital as it moves in and out at the whim of the market. From this view, therefore, financial regulation and surveillance are only part of the answer to a much bigger question.

Looking at Asia, it is evident that uncontrolled and hysterical movements of private capital — both in and out — was one of the major causes of the economic meltdown. Governments in the region had been persuaded and encouraged by the World Bank and the IMF that financial liberal-

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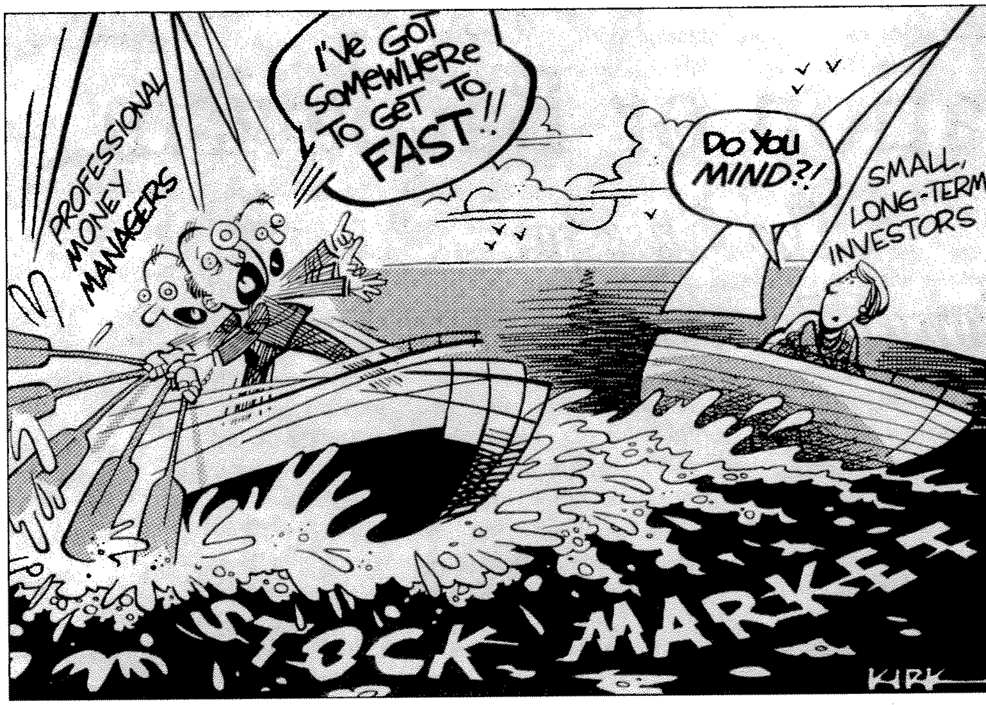
ization, backed by pegged currencies, was necessary to suck in the foreign capital to fuel growth. Therefore, they liberalized their capital accounts and backed their currencies, clinging to both poles of the policy doctrine long after either was a sound option. But repeated currency attacks and uncontrolled capital flight eventually forced dramatic currency devaluations, plunging these economies into debt and recession. It became clear very quickly that financial liberalization is a revolving door, that money can go out just as easily as it comes in.



THE DEMOCRACY DEFICIT

Beyond the simple economic causes and effects of the Asian crisis is an underlying problem which exists at every level, and which is central to any discussion about the need for a new global economic order, and what it should look like. And that problem is democracy — or more accurately, the lack of democracy.

Locally and nationally, governments pursued export-oriented development which largely benefited an elite, deepened inequities and destroyed the environment. The economic crisis has simply exacerbated existing problems and rolled back the not insignificant gains of the past 20 years. It has also shown the fragility of these gains.

Nationally and regionally, elites defended their behavior in terms of cultural relativism — dismissing anyone who criticized their authoritarian ways as cultural imperialists imposing Western values. For their part, Western capitalists, governments and multilaterals were complicit: rapid growth, expanding markets and political "stability" was the perfect combination to fuel global growth and create mutual benefit between the elites of the North and South.

In this respect, the North's abandonment of President Suharto is staggering in its hypocrisy. His authoritarian credentials were well-established and human rights groups in Indonesia and internationally consistently raised well-founded concerns over issues such as repression of the Aceh independence movement, the colonization of East Timor and the state's overwhelming coercive powers. However, it was only when Suharto showed his economic incompetence, or obstinacy, by not bowing to the IMF, that the West pulled the rug out from under him.

Internationally, the institutions which are steering the global economy are secretive, ideological and incapable of dealing with the complexity of the problems that the world confronts today. None more so that the IMF which, through its misguided prescriptions and repeated blunders in Asia, has shown that its ideological blinders render it incapable of responding to complex, diverse and volatile situations. Nor does it learn from experience, as the latest debacle in Russia has shown.

The World Bank, for all its breast beating and reformist rhetoric, is equally culpable. If there was any intellectual integrity in that organization, it would make a clean break from the IMF and simply refuse to clean up the Fund's mess. The World Bank's social safety nets are nonsense, especially when the need for them can in large part be traced to the incompetent and recession-inducing policies of its sister organization. In addition, they are pitifully small amounts compared to the needs created by the crisis. The fact that governments have to borrow additional money for these programs just adds salt to the wound.

But, the democracy deficit is most staggering in the financial sector — commercial banks, mutual and pension funds, currency speculators, finance companies, security traders, merchant bankers, stock analysts, investors, brokers, bonds dealers. These are the faceless, nameless players who operate in the shadows, beyond accountability except, possibly, to their shareholders and investors. According to economic theory, they take the risks, and either reap the profits or bear the loss. But, as seen in Asia and elsewhere, the private sector made the profits and, for the most part, was able to pass the losses to the public sector, thanks to the IMF. That's one way of spreading the risk.

However, the IMF cannot go on bailing out investors forever, hence the call for a market-based mechanism to reduce risk. Regulation of this kind — for example through better surveillance and disclosure — might make the market work better, but there is precious little evidence to show that the market — as presently constructed — makes things better for the vast majority of the world's population.

Nonetheless, certain kinds of regulation and institution building are integral to expanding political participation and economic democracy. Regulation should be a tool which allows local communities, national governments and regional groupings to manage their economies in the interests of their populations, and a means of ensuring the accountability of institutions and governments to their populations.

There is no silver bullet.

SEEKING DEMOCRACY — AT THE NATIONAL LEVEL

Although we are facing global economic problems, we would be foolish to pin our hopes on a "global" solution. Activists spend a great deal of time critiquing and attempting to reform the international institutions of economic globalization — the World Trade Organization, the International Monetary Fund and World Bank. These institutions are not accountable, they are not democratic and they consistently favor the strong over the weak and the rich over the poor. There is no reason to believe that an international regime charged with regulating financial movements would be any different — we would end up with yet another multilateral organization, dominated by the G7, with a mandate to do little more than take some of the risks out of the market and bully recalcitrants like Malaysia's Mahathir into towing the line. And activists will have to spend the next 20 years working out what on earth they are doing, telling them they should consult more with NGOs, and arguing for social and environmental conditionalities. It is a waste of our time, and doesn't solve the problem.

We must take a radical approach which is grounded in a fundamental commitment to increasing political participation for all people and economic democracy for all people.

While some solutions may be best applied internationally — for example, a Tobin Tax on all international currency transactions — many, and probably most, solutions can only be worked out and implemented locally, nationally and regionally. That is, power over economic policy must be handed back to people and their governments. For the past 15 years — certainly since the Latin America and Africa debt crisis — the IMF, the World Bank, the U.S. government, the European Union and multinational corporations have systematically stripped developing countries of their economic sovereignty. At the same time, the progress of democratization in many developing countries has been painfully slow. These two things are not unrelated. The impoverishment and indebtedness caused by structural adjustment programs and the obsession with growth encouraged by the IMF and World Bank, has sucked power away from people.

THE POWER OF MONEY

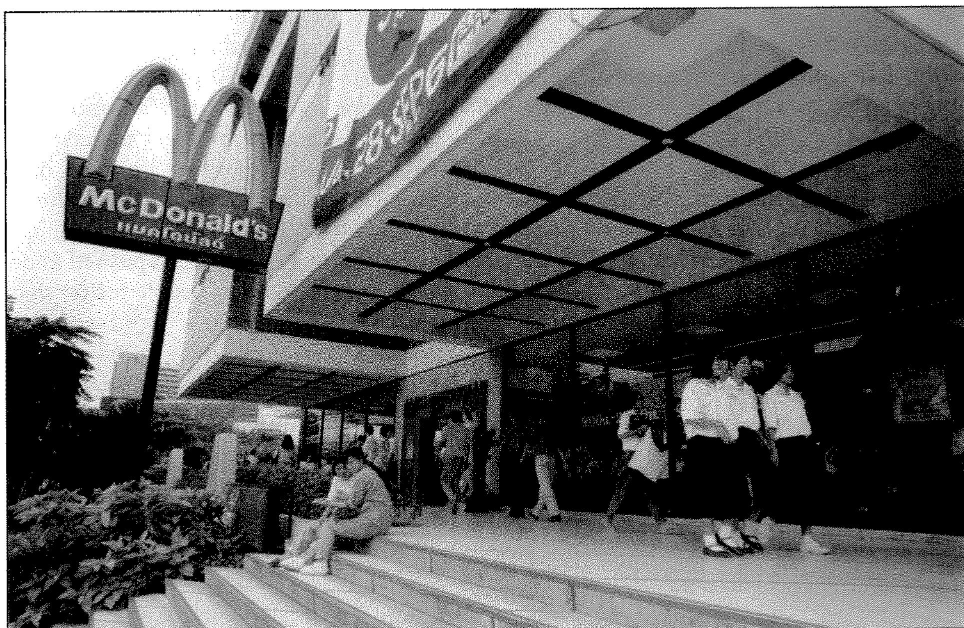
Economic power is real power — as we have seen all too clearly in Asia. The governments of Asia's tiger economies had power so long as their growth rates were booming. They were able to put the democratic aspirations of their populations on hold by promising economic prosperity. Of course, this was not accepted without struggle and in Thailand, for example, the democracy movement has made tremendous progress in the past 20 years.

But in late 1997, investors and speculators stripped that "power" away from governments as soon as they pulled their money out. In Indonesia, the consequences are most dramatic and the economic and political crises have become indistinguishable from each other. In Thailand, the Philippines and South Korea, governments have been pushed aside and replaced. Still, disillusion is evident as people realize that even their new, more democratic governments have ceded economic sovereignty to the IMF and that they respond more to the directives of IMF letters of intent than to the mass protests of landless farmers and laid-off workers. There is something wrong with this picture.

Selling fruit in Thailand.

In thinking about regulation and a "new global financial architecture," it is important to ask what we are hoping to achieve. If the answer is simply to avoid "aberrations" — such as the Asian economic crisis — in the forward march of economic globalization then we are on the wrong path. If the answer is regulation as a means of reconstructing global economic relations, for the purpose of creating greater intra- and inter- national democracy, then we need to go back to the drawing board and start again.

The basis for our design should be increasing political participation, economic democracy and social justice. This means pushing decisions down the "food chain." Minimally, it means stripping the IMF of its assumed power to impose policy conditions on governments. Minimally, it means allowing governments to establish whatever kinds of barriers they think are necessary to protect their domestic economies from the unpredictable global economy. Minimally, it means recognizing that there is no single solution, no single approach to achieve sustainable development.



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McDonald's in Bangkok.

The results will be messy, sometimes idiosyncratic, incremental, a pain in the neck for multinational corporations and anathema to the zealots of economic globalization.

But, the global economy needs to be deconstructed and built again on a sound moral basis of equity and sustainability. No amount of tinkering and reform of the existing global financial architecture will get this result. No amount of surveillance and disclosure will put economic power back into the hands of the mass of people.

GETTING RID OF HOT MONEY

We have to do a lot more than "cool down hot money" — we have to get rid of it and discredit the whole notion that there is anything useful in speculation. The financial market, as it presently operates, serves very little useful purpose and is, for the most part, non-productive. It does not create anything that you can eat or hold or sell or use. It does not add to the public good, and it distorts our collective understanding of what is valuable and productive.

One of the ways of cooling down hot money is to redirect it into productive channels. And here is one of the great conundrums of the present economic system: the massive accumulation of finance and speculative capital is due to overproduction — a bewildering concept considering that we live in a world where four-fifths of the population struggles daily with poverty. The massive profits of multinational corporations and banks have nowhere "useful" to go, so they go into speculation. In addition, corporations make such stupendous profits that they have diminishing need for traditional banking services, so banks have found new ways of making profits by diversifying into securities and non-foreign direct investment activities. This explains the appearance of incomprehensible financial instruments which manipulate and capitalize on the cracks in the market to make quick profits. In addition, the massive growth of pension and mutual funds — due in large part to the privatization of social security and the individualism inherent in neo-liberal economics — has created an enormous pool of highly mobile capital in search of maximum return.

But the other side of overproduction is demand, and here is the key. A stunningly simple solution to the problem of excess profits, is to expand markets — that is, to put more money in the hands of more people, so that they can buy the simple, basic life-enhancing consumer goods that countries like Vietnam, China, Thailand and Brazil are so good at producing. The good news for the United States is that it does not need to shoulder the burden of consuming the world's output on its own!

Redistribution of wealth and purchasing power to the four-fifths of the world which is not being given a chance to pull us out of this recession would give the economy a kick start, would ease the problem of overproduction, and provide all sorts of useful ways to recycle profits. It would also cool down global capital markets.

However, creating this demand requires significant social reform in terms of asset and income distribution — it means land reform and wage and labor reform. Industrialization via cheap labor and natural resource exploitation is no longer viable. We have reached the point where further economic growth can only be achieved by expanding domestic markets and by expanding our definition of what is productive to include public goods, culture, the environment and human security. We are at a moment in history where economic necessity coincides with social justice. ■