Ending Wall Street's Reign

For nearly two decades, the world has lived under the reign of Wall Street. It is now clearer than ever that the king must be dethroned, and the people made sovereign.

There are certainly many contributing factors to the economic crises which have spread in the past year throughout Asia, moved to Russia and which now threaten much of Latin America and South Africa. But atop the list is "hot money" — foreign loans and investments which pour especially into developing countries in pursuit of high returns but pull out at the first sign of economic downturn.

In the last two decades, countries around the world have opened themselves to "hot money" under pressure from the International Monetary Fund (IMF) and in response to a near-consensus among establishment economists, Wall Street advisers, aid agencies and development analysts that openness to unregulated capital inflows and outflows is the only path to economic salvation.

The last year has shown, instead, that failing to regulate capital flows invites economic ruin. The basic problem is that, when foreign lenders and investors fear a country may have difficulty paying back loans, they flee en masse. With investors overwhelmingly seeking to exchange their rupiah or ringgit or rubles for dollars or other dependable currencies, the value of the developing country currency plummets, throwing the country into economic crisis. For all the differences between Thailand, South Korea and Russia, they have all suffered from this phenomenon.

With developing countries across the globe facing enormous uncertainty, two developing nations stand out for having weathered the economic storms better than most: Chile and Taiwan.

Their common trait? Both impose meaningful capital controls. In Chile, foreign investors have faced a stiff tax if they withdraw their money less than a year after putting it in the country — though the IMF has lobbied successfully for Chile to water down this rule. In Taiwan, a mix of government measures — including instructions to banks not to lend local currency to foreign banks and requirements that corporations report any large sums they are taking out of the country — has stabilized the New Taiwan dollar, a feat the conservative Economist magazine calls "an extraordinary achievement."

Now Malaysia is looking to follow suit. On September 1, Malaysian Prime Minister Mahathir Mohamed announced that the government would establish a fixed exchange rate for the local currency, the ringgit. Malaysia is requiring the repatriation of all ringgit within one month, and afterwards will not honor ringgit outside of the country as good currency. Accompanying these measures are severe limitations on Malaysians' ability to move ringgit out of the country, for investments or even in connection with personal travel.

"What is obvious is that people can no longer stay with the so-called free market system," Mahathir said in an interview with the Malaysian newspaper *The Star*. "The ringgit cannot be traded at all so that we can regain control over the exchange rate involving our ringgit." The goal, he explained, was to reduce the uncertainty caused by speculation.

"We have asked the International Monetary Fund to have some regulation on currency trading but it looks like they are not interested," Mahathir said.

Mahathir acknowledged that the currency regulations were likely to cause some transaction costs for businesses that would need permission to acquire currency for international trade, but he argued that these costs would be more than offset by the benefits of stability expected from the new regulations.

The Wall Street/IMF approach has considered these kinds of measures a retrograde throwback to the days of command economies. But with the recklessness and failures of the Wall Street unregulated globalization approach now apparent, countries are likely to become increasingly willing to reject the orthodoxy.

One particularly meritorious idea is the "Tobin Tax," named for Nobel laureate James Tobin, which would place a tax on international currency transactions as a way to discourage rapid churning in the currency markets.

The Tobin Tax, the Chilean, Taiwanese and Malaysian plans and many other proposals for capital controls all deserve immediate and serious consideration around the world.

One of the unfortunate consequences of the near universality — until recent months — of the faith in open, unregulated financial markets is the dearth of experiments in imposing capital controls, or even academic theorizing on the matter. Surely there is no guarantee that any particular approach will work for any particular country, or for all countries.

Nonetheless, it is clear that reclaiming citizen sovereignty from Wall Street and its equivalents in Tokyo, Frankfurt, London and elsewhere will require subordinating the needs of finance to those of people, and imposing controls on the flow of money to protect national economies. ■