The Globalization Gamble: The Dollar-Wall Street Regime and its Consequences. By Peter Gowan

The 1990s have been the decade of globalisation. We see its effects everywhere: in economic, social and political life, around the world. Yet the more all-pervasive are globalisation's effects, the more elusive is the animal itself. An enormous outpouring of academic literature has failed to provide an agreed view of its physionomy or its location and some reputable academics of Right and Left even question its very existence. Others, notably Anglo-American journalists and politicians, insist it is a mighty beast which savages all who fail to respect its needs. They assure us that its gaze, 'blank and pitiless as the sun', has turned upon the Soviet Model, the Third World Import-Substitution Development Model, the European Social Model, the East Asian Development Model, bringing them all to their knees. For these pundits, globalisation is the bearer of a new planetary civilisation, a single market-place, a risk society, a world beyond the security of states, an unstoppable, quasi-natural force of global transformation.

Yet, as the East Asian crisis turned into a global international financial scare, some who might be thought to be deep inside the belly of this beast, the big operators on the 'global financial markets', wondered whether globalisation might be in its death agony. At the start of 1998, Joe Quinlan, senior analyst for the American investment bank Morgan Stanley, raised the possibility that globalisation may be coming to an end. He noted that "globalisation has been the decisive economic event of this decade" and stressed that "no one has reaped more benefits from globalisation than the United States and Corporate America....The greater the velocity and mobility of global capital, the more capital available to plug the nation's low level of savings and boost the liquidity of financial markets. In short, globalisation has been bullish for the world economy in general and for the United States in particular." But Quinlan worried that governments in various parts of the world may be turning against globalisation and may decide to bring it to an end in 1998. As he put it: "...the biggest risks to the world economy next year is not slower growth, but rather an unravelling of global interdependence -- and therefore the end of globalisation."[1] For Quinlan, then, globalisation is a rather fragile, vulnerable creature, dependent upon the nurturing care of states.

Thus, we are left with an awareness that there have indeed been powerful new forces in the international political economy of the 1980s and 1990s, which we label globalization, but their contours, dynamics and causes remain obscure: as elusive to our grasp as a black cat in a dark room.[2]

This essay is yet another attempt to catch this cat called globalization, or rather to catch one of its main organs: its central nervous system. We will argue that this lies in the way in which international monetary and financial relations have been redesigned and managed over the

[1] Joe Quinlan: "Devaluations, Deficits and the End of Globalisation?", Morgan Stanley Global Economic Forum, The Global Economics Team, Special Year-End Issue, 22nd December 1997 (Morgan Stanley & Co., New York,1997)

[2] I must acknowledge the source of this metaphor in an excellent joke by Professor Wagener at a recent conference in Berlin. The joke goes as follows: economic history is chasing a black cat in a dark room; economics is chasing a black cat in a dark room when the cat isn't there. Econometrics is chasing a black cat in a dark room when the cat isn't there and you claim that you have caught it!

last quarter of a century. This new monetary and financial regime has been one of the central motors of the interlocking mechanisms of the whole dynamic known as globalization. And it has been not in the least a spontaneous outcome of organic economic or technological processes, but a deeply political result of political choices made by successive governments of one state: the United States. In this sense we are closer to the Morgan Stanley view of globalization as a state-policy dependent phenomenon than to the notion of globalization as a deep structure favoured by Anglo-American media pundits. To indicate its location in international reality we call it a *'regime'*, although, as we will explain, it is not a regime in quasi-juridical sense in which that word has been used in American international relations literature.

International monetary and financial relations are always the product of both economic and above all political choices by leading states. Studies of globalization which fail to explore the political dimensions of the international monetary regime that has existed since 1973 will miss central features of the dynamics of globalization. This international monetary regime has operated both as an international 'economic regime' and as a potential instrument of economic statecraft and power politics. The name given to it here is the 'Dollar-Wall Street Regime' (DWSR). We will try to trace its evolution from origins in the 1970s through the international economics and politics of the 1980s and 1990s up to the Asian crisis and the panic of 98.

We are not going to claim that the history of international monetary and financial relations of the last quarter of a century gives us the key to understanding the contemporary problems in the advanced capitalist economies. As Robert Brenner has demonstrated, these problems of long stagnation have their origins in a deep-seated crisis of the productive system of advanced capitalist societies.[3] The onset of this stagnation crisis formed the *background* to the changes initiated by the Nixon administration in international monetary and financial affairs: but the production crisis did not determine the *form of the response.* There were a range of options for the leading capitalist powers to choose from and the one chosen, which has led to what we call globalization, was the outcome of international political conflicts won by the American government. Since the 1970s, the arrangements set in motion by the Nixon administration have developed into a patterned international regime which has constantly reproduced itself, has had very far-reaching effects on transnational economic, political and social life and which has been available for use by successive American administrations as an enormously potent instrument of their economic statecraft. One of the most extraordinary features of the whole story is the way in which these great levers of American power have simply been ignored in most of the literatures on globalization, on international regimes and on general developments in the international political economy.[4]

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[3] See the superb analysis in Robert Brenner: "The Economics of Global Turbulence", New Left Review 229,1998.

[4] The major exception to this blindness has been the work of Susan Strange who constantly sought to educate us on the politics of international monetary and financial affairs and whose great classic, Sterling and British Policy, remains the indispensable starting-point for thought about the interaction of international politics, money and finance.

In exploring this Dollar Wall Street Regime we need no algebra or geometry and almost no arithmetic or even statistics. The basic relationships and concepts can be understood without the slightest familiarity with neo-classical economics. Indeed, for understanding international monetary and financial relations, lack of familiarity with the beauties and ingenuities of neo-classical economics is a positive advantage.

The essay is in five parts. We begin with a brief discussion of terms, concerning the meaning of 'capital markets' and the roles and forms of financial systems. In the second part we look at the new mechanisms established for international monetary relations by the Nixon administration in the 1970s. The resulting regime gave leverage both to the US government and to Anglo-American financial markets and operators. One of the fascinating features of the regime is the way in which it established a dynamic, dialectical relationship between private international financial actors in financial markets and US government dollar policy. Most of the literature on globalization tends to take as a governing assumption the idea that the relationship between the power of markets (and market forces) and the power of states is one mainly marked by antagonism -- an idea deeply embedded in much liberal thought.[5] Yet, in a seminal article written at the time of the Nixon changes, Samuel Huntington noted how false that idea is: "Predictions of the death of the nation-state are premature....They seem to be based on a zero-sum assumption...that a growth in the power of transnational organisations must be accompanied by a decrease in the power of states. This, however, need not be the case."[6] We try to show how the DWSR, steered by the US government, worked in and on the international political economy and how it latched onto and changed the internal economics, politics and sociology of states and their international linkages.

The third part of the essay looks at the operations of the Dollar-Wall Street Regime over the last quarter of a century. We look at how US administrations have sought to use the regime, and the responses of the European Community states, Japan, the countries of the South and of the former Soviet Bloc to the regime. We also look at how the regime contributed towards changing the US domestic financial, economic and political systems.

In the fourth part, we try to place the DWSR and its effects into the framework of the dynamics of international politics as a whole in the early 1990s. We look at these issues, so to speak from the angle of the lead state: the United States. And we try to build in the effects of the Soviet Bloc collapse on how American leaders formulated their strategic goals and recombined their tactics. I argue that they rationally had to, and did, recognise that their key challenge lay in East and South East Asia. And to tackle that challenge and to frustrate future challenges to US global leadership, they had to radicalise the DWSR and seem to have used it as an instrument of economic statecraft in East Asia.

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[5] I do not wish to suggest that tensions between the goals of governments and the dynamics of markets are not an important object of investigation. See Robert Boyer and Daniel Drache (eds.): States Against Markets. The Limits of Globalization (Routledge,1996)

[6] Samuel Huntington: "Transnational Organisations in World Politics", World Politics, 25, April 1973.

In the fifth part we argue that the conventional view of the unfolding of the central drama of East Asian crisis in the autumn of 1997 -- the events in South Korea -- is mistaken insofar as it assumes the central actors to have been market forces. The critical role was played by the US Treasury, which acted in quite new ways during the Korean crisis. It was this Treasury intervention in South Korea which was responsible for the subsequent Indonesian collapse and which indirectly and unintentionally set in motion the triggers which turned the East Asian crisis into a global financial crisis during 1998. At the same time, the reason why the US Treasury's action could play this triggering role lay in the effects of 20 years of US exploitation of the Dollar-Wall Street Regime on the world economy. We conclude by considering whether there is a possible social-democratic capitalist alternative strategy which could reverse the dynamics of globalization.

PART ONE: 'CAPITAL MARKETS', FINANCIAL SYSTEMS AND THE POST-WAR INTERNATIONAL MONETARY SYSTEM

Most of the various notions of what globalization is about focus on the growing mobility of capital across the globe in the 'global capital market' and upon the impact of this mobility on national economies. But the term 'capital market' is analytically incoherent, because it embraces radically different phenomena in the field of finance, most of which have nothing directly to do with capital in the usual common sense meaning of the term, while at the same time it excludes a great deal of the operations of what capital actually does. So we need to clarify our notions about 'capital markets', global or otherwise, in order to understand this international phenomenon known as globalization.

The So-Called Capital Markets

In common sense language we associate the word capital with the idea of funds for productive investment, for putting together machines, raw materials and employees to produce sellable items. This is a useful starting point for using the word capital because it stresses its socially beneficial role within a capitalist system.

One of the central confusions concerning globalization lies in the widespread belief that the so-called 'global capital markets' in which trillions of dollars are bouncing back and forth across the globe are in some way assisting the development of the productive sector of capitalism. It is because we imagine that the 'global markets' are integral to production that we imagine that we have no choice but to accept them. Yet in reality the great bulk of what goes on in the so-called 'global capital markets' should be viewed more as a charge upon the productive system than as a source of funds for new production. The idea that the current forms of 'capital markets' are functionally indispensable investment mechanisms is a serious error. The 'capital market' is both much more and much less than the funnel for productive investment. It is much more because it includes all forms of credit, savings and insurance as well as large, diversified markets in titles to future income and not just credits for productive investment. And it is much less because very large flows of funds into productive investment do not pass through the so-called 'capital markets' at all.

This confusion about the role of capital markets is linked to another, concerning 'mergers and acquisitions. Thus, it is often assumed that when one company buys control of another company, some kind of capital investment is taking place. Yet frequently such acquisitions of assets may have nothing to do with new real investment at all, indeed, the reverse may be occurring: the acquisition may be concerned with running down the activities of the acquired asset, in order that the buyer of the asset can eliminate competition and gain greater market power. During the last quarter of a century this process of 'centralisation of capital' has been proceeding apace internationally. It is called 'Foreign Direct Investment' but in most cases it simply means changing the ownership of companies and may have to do with disinvestment in production rather than the commitment of new resources to expansion of production.

The notion that a great expansion of the size of 'capital markets' is a symptom of positive trends in capitalist production is as false as imagining that a vast expansion of the insurance industry is a sign that the world is becoming a safer place. Insurance can operate in the opposite way: the more crime the bigger the property insurance market. Similarly, when great fortunes are being made overnight on 'capital markets' the most useful rule of thumb for interpreting such trends is one which says that something in capitalism is functioning very badly from a social point of view. We will explore some of these terms, starting with the most obvious feature of financial systems, their role in supplying credit.

Credit involves lending money to people on the understanding that they will pay the money back later along with a bonus or 'royalty', usually in the form of a rate of interest.[7] There is nothing necessarily capitalist about credit and large parts of national credit systems are not related to production at all. Workers can put their savings into a credit co-operative and draw loans from it in hard times in the hope of paying the money back in better times. They pay a royalty for the service but this can be small because the co-operative is non-profit-making. Such co-operatives serve consumption needs, not production and they are not capitalist. Building societies confined to the housing market play a similar role in supplying credit for people to purchase housing. A common feature of these kinds of organisations is that the credit-money that they issue is directly derived from savings deposited within them. In other words, their resources come from the past production of value in the economy: employees' savings come from wages that they have already earned in production.[8]

[7] The term 'royalty' covers interest, ground rent, taxes, financial service fees and dividends. I derive the term from Shaikh and Tonak (though they do not include dividends in their definition. See Anwar M.Shaikh and E.Ahmet Tonak: Measuring the Wealth of Nations. The Political Economy of National Accounts (Cambridge University Press,1994).

[8] Throughout this article, the term 'production' refers to those activities that produce use-values. Not all such production in capitalist societies is controlled by private capital: eg, cooking or the supply of housing may not be. But the bulk of the productive sector will be. On the definition of this term, see Anwar M. Shaikh and E.Ahmet Tonak, op. cit.

Banks are different because they are able to *create new money* in their credit operations. We can see this when we realise that at any one time, the banks as a whole could be giving overdrafts to everybody in the entire economy. Thus, far more money is circulating in the economy than the money derived from savings generated by past value creation. Part of the money is actually what we can call fictitious money -- money derived not from the past but from expectations that it will be validated by future productive activity.[9] Within capitalism, banks also do not have to be operated as private capitalist companies. At the beginning of the 1990s, for example, more than half of the 100 biggest banks in Europe were publicly owned and their financial criteria for operating were, in principle, matters of public choice. And even if they are private, the banks play such an essential and powerful role in the public economy because of their capacity to issue credit money that any sensible capitalist class will ensure that the state is constantly interfering in their operations (even though, for ideological reasons, one wants to keep these state functions 'low profile'). As Kapstein puts it: "Banks are told how much capital they must hold, where they can operate, what products they can sell, and how much they can lend to any one firm."[10]

The existence of this fictitious credit money is very beneficial for the whole economy because of its role in facilitating the circulation of commodities. Without it, economic development would be far slower. It is especially important to employers, enabling them to raise large amounts of money for equipment which will yield up its full value in production only over many future years. If employers could invest only real savings -- the money derived from past value-creation -- investing in fixed capital would be far more costly --too costly for a lot of investment. And credit has also become a very important means of expanding the sales of goods to consumers. This is another way of saying that modern economies run on large amounts of debt. So the banks do play an important role in both channelling savings and creating new funds (fictitious money) for productive investment. An entire capitalist economy could be run with a financial system consisting entirely of such banks.

But historically, other forms of financial institutions have grown up, especially in the Anglo-Saxon world which has played such a central role in the historical development of capitalism. First there has been the development of shares and bonds as means of raising funds. A company can offer shares for sale and use the funds from the sale to invest in the business. The shares are pieces of paper giving legal titles to a claim on future profits from the company's activities. Companies or governments can also sell bonds and use the funds from the sale for an infinite variety of purposes. These bonds are similarly pieces of paper giving legal titles to a fixed stream of future income to the holder for a fixed period of time. A special feature of shares and bonds (known collectively in England since the 18th century as 'stocks') is that secondary markets have grown up enabling people to buy and sell these pieces of paper entitling the holder to future royalties. Today there are all kinds of pieces of

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[9] See Bob Rowthorn: Capitalism, Conflict and Inflation (Lawrence and Wishart, 1980) and David Harvey: The Limits of Capital (Blackwell,). Harvey's very important book provides an excellent survey of the roles of finance within capitalism.

[10] Ethan B. Kapstein: Governing the Global Economy. International Finance and the State. (Harvard University Press, Cambridge Massachusetts, 1994)

paper that can be bought and sold and that entitle the holder to some kind of future royalty or right. I can buy and sell paper giving me the right to buy or sell a currency at a certain rate at a certain time in the future. There has been a huge growth in markets for such paper claims. The generic term for all such tradeable pieces of paper is ‘securities’.

It is important to recognise that while the initial issuing of a set of shares or bonds *is* a means of raising funds that may (or may not) be used for productive capital investment, the secondary markets in these securities are not contributing directly at all to productive investment.[11] Instead the people on these markets (such as the Stock Market) are buying and selling ***claims on future value created in future productive activity.*** They are not handing over funds for that productive activity; they are claiming future royalties from it. These claims on future royalties from future production are either direct or indirect claims. A share in Ford Motors is a direct claim on future value created in Fords. A Russian government bond which I hold is an indirect claim on future Russian production of value. I hold the bond not because I think the Russian government will produce the value but because I imagine that it will pay me my royalty by extracting taxes from the productive activity of others in Russia: no production, no royalty on my bond.

Against this background, we can now return to the phrase ‘capital market’. What is mainly (although not only) referred to by this phrase is actually *securities markets*. And we thus discover that ‘capital market’ in the sense of a securities market may have nothing directly to do with supplying funds for capital investment. It may have to do with the opposite process: trading in claims to draw profits *from future productive value-creation.* At the same time, both bank credits and bonds may be used for capital raising functions but they may equally be used for other purposes. And neither foreign exchange markets nor the so-called derivatives markets have anything directly to do with capital investment -- we will examine later what their functions are.

How could such an apparent abuse of language, whereby various kinds of financial markets are all described as capital markets, occur? The answer is that it is not an abuse of language for one group of the population: rentiers and speculators. Rentiers are those who derive their income from extracting royalties from future production. The speculators are those who derive their income from trading in securities or currencies by trying to sell them at higher prices than they bought them for.

As has been implied by our analysis, rentiers are not, in principle, an integral element in capitalism. Those parts of the system’s reproduction which necessarily involve the channelling of funds of money from past value-creation and from credits in the form of fictitious money could be handled entirely by commercial banks (which could themselves be publicly owned).

Thus, when we examine the growth of the so-called ‘global capital markets’ we will find that

[11] The economic justification for these ‘secondary markets’ is that their existence facilitates the search of companies and governments for buyers of their offerings of shares or bonds: they buyers have the safety of knowing that they can sell their bonds or shares easily later on the secondary markets.

much of their activity is not about the supply of capital for productive activity. It is about trading in royalties on future production in different parts of the world or about businesses engaging in various kinds of insurance against risks. And the trend in the organisation of the flows of finance has been increasingly one which privileges the interests of rentiers and speculators over the functional requirements of productive investment. This fact is revealed through an examination of the tensions between what we may call the two poles of capitalism, that of money-dealing capital and that of the employers of capital in the productive sector.

The Two Poles of Capitalism and Their Regulation

Whether the financial system is organised predominantly in the form of commercial banks or in the form of securities markets, we notice a division which is inherent in capitalism: the division between money-dealing capital on one side and productive capital on the other. These two entities have different kinds of concerns because of the different circuits of their capitals. For the employer of capital in the productive sector the circuit runs as follows: capital starts as money (some of which is borrowed from the money-capitalist), which is then turned into plant, raw materials and employees in the production process. The capital then emerges from production as a mass of commodities for sale; when the sale is completed capital re-appears in the form of money with the extra-surplus extracted from the production process. Out of this extra surplus, the employer of capital pays back the money-capitalist the sum initially advanced, along with royalties.

But from the angle of the money capitalist, the circuit looks different. It starts with a fund of money. This money is then locked into a project for a certain time. At the end of that time, the money capitalist hopes to get the money back with a royalty. For the money-capitalist absolutely any project which will offer a future royalty is what capitalism is all about. If buying a share in Fords gives a royalty of 6% in a year, while a Ukrainian government bond will give a royalty of 34% and buying a case of Chateau Lafite to sell it in a year will yield 15%, the problematic is the same for the money capitalist in each case: in an uncertain future, which of these different 'capital markets' will give me the best mix of safety and high yield?

Property that can be used as capital thus appears simultaneously in two polarised embodiments: on one side stand the *money capitalists* controlling enormous accumulations of funds; and on the other side stand the *employers of capital* managing the enterprises. These are two forms of the same thing, analogous to God the Father and God the Son. But their polarisation is very important because it enables money capital as the controller of funds to play a planning role in capitalist development. By being distanced and relatively autonomous from the employers of capital in the productive sector, the money-capitalists can pick and choose what sectors they advance money capital to. If a branch has reached 'maturity', barely achieving the average rate of profit, then resources of value from that sector as well as fictitious money can be advanced to other sectors which seem likely to produce higher rates of return. Through such redeployments, the financial system in the hands of the money-capitalists is supposed to spur growth.

For supporters of capitalism this development co-ordination role of the money capitalists is considered to be one of the most ingenious and beautiful aspects of the entire system. One might say that the relationship between the productive sector and the financial sector is one where the productive sector is determinant but the financial sector is dominant. The productive sector is determinant because it produces the stream of value out of which the money-capitalists in the financial sector ultimately gain their royalties, directly or indirectly. On the other hand the financial sector is dominant because it decides *where it will* channel the savings from the past and the new fictitious credit money -- who will get the streams of finance and who will not. The actual power balances between the two sectors are partly governed by the business cycle. In the boom productive capital is flush with cash and can, so to speak dictate terms to the money capitalists; but in the recession the money capitalists become ruthless, bullying tyrants as the employers of productive capital beg for credit to tide them over. But power relations between the two are also crucially affected by institutional design -- by the social relations of production. The state, through a highly charged and politicised process, can and does tilt the balance between the money-capital pole and the productive capital pole and between the money-capital pole and all parts of the credit system, keeping, for example, money-capital out of whole sectors of the credit system, if it wants to. The state also makes crucial decisions about the internal structure and inter-actions within the money-capital pole itself. What will banks be allowed to do, and what will they be kept out of? Will we have a private securities market or not? And so on. And we must also remember that the state is not just designing relations between the two poles of capital; it is also designing its own relation with the financial pole because it too will wish to use the credit system.

From our analysis of these two poles of capital, another very important distinction emerges, between the tempos and rhythms of two kinds of financial flows linked to the two different kinds of circuits. For the money capitalist there is a tendency to seek quick returns and to keep capital in as liquid a state as possible, for reasons of safety. The employer of capital seeks to set up much longer-term circuits, particularly concerning funds for fixed capital investment, which yield their full value only over many years. The tendency for the first group is thus to generate 'hot money' flows, extremely sensitive to even very small changes in their environment; while the second group tends to generate cold, long flows which have to be robust to significant changes in their environment. The hot flows are linked to royalty seeking from either securities trading or from very short-term loans. This difference is extremely important when we seek to analyse international movements of funds. Insofar as all kinds of money can flow freely internationally, we would expect to see very radical differences between these two kinds of flows: a small change in the exchange rate of one country or in the short-term, government-fixed interest rates in another can produce sudden, major shifts in flows of hot money, but exert no significant influence on flows of funds concerned with real, long-term investment in production.[12]

The relationship between capital and labour within the productive sector is, of course, an absolutely fundamental social relationship in the functioning of any actual capitalist system. But the relationship between money-capital and the productive sector is another absolutely central social relationship. Some of the sharpest conflicts within capitalist societies have occurred around these social relationships between the financial sector and the rest of society.

[12] For further discussion on these differences, see G.Epstein and H. Gintis: "International Capital Markets and National Economic Policy", Review of International Political Economy, 2:4, Autumn, 1995.

At the end of the war, politics in the Atlantic world was governed by forces who favoured what the neo-liberals call ‘financial repression’ and what Keynes approvingly referred to as ‘euthanasia for the rentiers’. The story of the last quarter of a century has been that of the resurrection of the rentiers in a liberation struggle against ‘financial repression’. This has gone hand in hand with the idea that the approach to the design of financial systems championed by people like Keynes and the US occupation regimes in Germany and Japan after the war -- ‘financial repression’-- is an approach alien to genuine capitalism, apparently of Far Eastern origin! These debates concern not only the institutional-power relations between money-capital and the employers of capital but also the role of the state and the forms of class relationships across the entire society.

But to understand this whole story we must appreciate that these social and institutional design issues are not necessarily resolvable at a purely national level. It is actually an activity *also of the inter-state system, insofar as funds can flow more or less freely from one national currency zone to another*. For the money capital pole plays its role only through acting as money. And insofar as the currencies of states are more or less freely convertible by private economic actors into the currencies of other states, financial relations in one capitalist society can be subjected to powerful influences from the financial sectors of other capitalist states.

The transformation of the relations between the money-capital pole and the productive sector of national capitalisms has been a central feature of what has come to be known as ‘neo-liberalism’ over the last quarter of a century. But this transformation has been achieved in close connection with profound changes in the field of international monetary and financial relations. Against this background, we will examine the international monetary system and how it relates to international and national financial systems.

The International Monetary System

The need for an international monetary system is not, in itself, something derived from capitalism. It arises from the political as well as economic fact that the world is divided into separate states with separate currencies and from the fact that groups within one state wish to do business with (and inside) other states. Historically, most of that international business has been concerned with trade in goods. The problem of international monetary relations arises in the first place over how two groups in different currency zones can buy and sell goods. One obvious way of handling this problem is to use neither of the currencies of each state but instead to use a third form of money, say gold, which has an exchange price with each of the two currencies. Alternatively, there may be an established exchange rate directly between the two currencies and the seller of the goods may be prepared to accept payment in either of the two currencies, etc. The important point, for the moment, is simply that some sort of international monetary system is necessary for the functioning of an international economy.

These exchanges in the international monetary system are monitored closely at an inter-state level to answer one important question: are the economic operators of a state buying more from other states than they are selling to other states? In other words, what is a state’s so-called balance of payments in current transactions? Is the account in surplus or in deficit? These questions are important because if a state is heavily in deficit people start to wonder whether it will be able, in the future, to find the internationally acceptable money that it will need to pay all its international obligations. Does a deficit state have enough reserves of international money to keep paying off its deficit? Can it borrow internationally acceptable money from somewhere to keep meeting its obligations? The more such doubts grow, the more the economic operators within the state concerned can face difficulties of one kind or another.

But this system is not a 'natural' or a purely economic one. It is both economic and political. The whole concept of the balance of payments rests on the political division of the world into different states with different moneys. The arrangements for establishing acceptable forms of international money are also established by political agreement among states. And the treatment of countries with current account deficits or surpluses is also politically established. Should there be an arrangement whereby states with current account deficits cut back on their purchases from abroad to get rid of their deficits? Or should the surplus states be pressurised to buy more from the deficit countries? Arrangements of either sort can be put in place. If the deficit countries must adjust, that will have a depressive effect internationally, because they will cut back on their international purchases. If the opposite approach is used, it will have a stimulative effect on international economic activity.[13] Which approach is adopted will depend upon international political agreement between states over the nature of the international monetary regime that is to operate. And this agreement will not be one between equals. The biggest powers, or perhaps even one single big power, can lay down what the regime will be. All the other states will be 'regime takers', rather than 'regime makers'.[14]

The Bretton Woods Regime for International Monetary and Financial Relations

The concerns of Keynes and Dexter White in their efforts to construct a new international monetary system for the post-war world were to construct arrangements which would privilege international economic development. This required a predictable and stable international monetary regime that would be rule-based and would not be manipulable by powerful states for mercantilist advantage.

They therefore retained gold as the anchor of the system -- a money separate from the currency of any nation state. And they laid down that the dollar would have its price fixed against gold. Other states then fixed their currency prices against the dollar and were not allowed to unilaterally change that price as they pleased. Changes in currency prices would be settled co-operatively between states through a supranational body, the International Monetary Fund. The result of these arrangements was that economic operators enjoyed stability in the prices of the main currencies against each other since all were fixed at a given price against gold. In practice, the dollar was the main international currency in use for trade, but its exchange price was fixed like that of any other currency.

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[13] Keynes had argued, in the Dumbarton Woods negotiations on the post-war international monetary system, that the surplus countries should adjust to ensure that the world economy was growth oriented.

[14] On these issues, see David Calleo and Susan Strange: "Money and World Politics" in Susan Strange (ed.):Paths to International Political Economy (Allen & Unwin,1984)

The second major feature of the Keynes-White system was that it largely banned private financial operators from moving funds around the world freely, giving the central banks of states great powers to control and prevent such financial movements. Private finance was allowed to transfer funds for the purposes of financing trade. There was also provision for funds to be moved across frontiers for foreign productive investment. But other movements of private finance were to be banned: 'financial repression' on an international scale. Such repression then meant that investment resources would be 'home-grown' within states. And it also meant that money-capital had to confine its royalty-seeking operations to those activities which its nation-state would allow. In other words, states were able to dominate and shape the activities of their financial sectors in ways that would suit the state's economic development goals.

This system seems to have worked very well, in terms of its growth record, even when most of the currencies of the advanced capitalist states were not even freely convertible with each other for current transactions (as was the case in Western Europe up to 1958).[15] But the regime was dismantled in the early 1970s by the Nixon administration, which thereby set the world economy on a new course. [16]

PART TWO: THE DOLLAR-WALL STREET REGIME

The New International Monetary System Created in the 1970s

In the early 1970s the international monetary system was radically transformed by the Nixon administration, in the teeth of opposition from all the other main capitalist powers.[17] We will not explore the whole context in which these changes were made, but it was one marked by very acute tensions between the United States and both Western Europe and Japan as well as by the debacle for the United States of its war in Vietnam. The tensions with its 'allies' derived essentially from the fact that both Japanese and West European capitals were not powerful enough to eat into markets previously dominated by US companies. In the monetary field the US was confronting a situation where, if the Bretton Woods regime was going to remain in place, the Nixon administration would have to arrange a substantial devaluation of the dollar against gold. Nixon opted instead to scrap Bretton Woods and to make a series of breathtaking moves to restructure international monetary and financial arrangements.

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[15] This is, of course, a highly 'stylised' picture of the regime, which was a good deal more messy than is suggested here. But we are concerned only to spell out general principles. For more detailed treatment of the origins and development of Bretton Woods regime see: Richard N. Gardner:Sterling-Dollar Diplomacy in Current Perspective (Columbia University Press, 1980); M. De Cecco: "The Origins of the Post-War Payments System" Cambridge Journal of Economics, 3, 1979; and Andrew Walter: World Power and World Money (Harvester Wheatsheaf, 1993)

[16] The crisis of the Bretton Woods system in the late 1960s and early 1970s is well covered in Ernest Mandel: Decline of the Dollar (Monad Press, New York, 1993)

[17] See John Williamson: The Failure of International Monetary Reform, 1971-74 (Von Nostrand Reinhold, New York,1977)

The Inauguration and Structure of the Dollar-Wall Street Regime
The Nixon administration imposed three key changes in international monetary relations: first, it ended the role of gold as a global monetary anchor, leaving the dollar as the overwhelmingly dominant international money. Now the only monetary units for international transactions were those paper moneys issued by states. This meant that the exchange price of the overwhelmingly most important international money, the dollar, untied to gold, could be decided by the US government.

Secondly the Nixon administration ended the previous rules of fixed exchange rates between the main currencies. It wanted to gain complete freedom for American administrations to establish the dollar's rate of exchange with other currencies as the US government wished: hence the end of fixed exchange rates. This was an enormously important development, because, for reasons which we will discuss later, the US government could, alone among governments, move the exchange price of the dollar against other currencies by huge amounts without suffering the economic consequences that would face other states which attempted to do the same.

And thirdly, the Nixon administration decided to try to ensure that international financial relations should be taken out of the control of state Central Banks and should be increasingly centred upon private financial operators. It sought to achieve this goal through exploiting US control over international oil supplies. It is still widely believed that the sharp and steep increase in oil prices in 1973 was carried out by the Gulf states as part of an anti-Israel and anti-US policy connected to the Yom Kippur war. Yet as we now know, the oil price rises were the result of US influence on the oil states and they were arranged in part as an exercise in economic statecraft directed against America's 'allies' in Western Europe and Japan. And another dimension of the Nixon administration's policy on oil price rises was to give a new role, through them, to the US private banks in international financial relations.

The Nixon administration was planning to get OPEC to greatly increase its oil prices a full two years before OPEC did so[18] and as early as 1972 the Nixon administration planned for the US private banks to recycle the petrodollars when OPEC finally did take US advice and jack up oil prices.[19] The Nixon administration understood the way in which the US state could use expanding private financial markets as a political multiplier of the impact of US Treasury moves with the dollar. But according to the Nixon's Ambassador in Saudi Arabia at the time, the principal political objective behind Nixon's drive for the OPEC oil price rise was to deal a crippling blow to the Japanese and European economies, both overwhelmingly dependent on Middle East Oil, rather than to decisively transform international financial affairs.[20] Nevertheless , Nixon's officials showed far more strategic insight into the

[18] See Terzian: OPEC: The Inside Story.

[19] See A.A. Kuburi and S.Mansur: "The Political Economy of Middle Eastern Oil", in GRD Underhill and R.Stubbs: Political Economy and the Changing Global Order (MacMillan,1994)

[20] See V.H.Oppenheim: "Why Oil Prices Go Up? The Past: We Pushed Them",

consequences of what they were attempting than most political scientists would credit any government with. Its capacity for deception both over the oil price rise and in the way in which it manipulated discussions with its 'allies' in the IMF over so-called 'international monetary reform' was brilliant.

Foreign Policy,25 Winter 1976-77. Oppenheim draws upon Nixon's Ambassador in Saudi Arabia, Akin, for her insight into the administration's thinking.

The US government realised that the oil price rises would produce an enormous increase in the dollar earnings of oil states that could not absorb such funds into their own productive sectors. At the same time, the oil price rises would plunge very many states into serious trade deficits as the costs of their oil imports soared. So the so-called petrodollars would have to be recycled from the Gulf through the Western banking systems to non-oil-producing states. Other governments had wanted the petrodollars to be recycled through the IMF.[21] But the US rejected this, insisting the Atlantic world's private banks (at that time led by American banks) should be the recycling vehicles. And because the US was politically dominant in the Gulf, it could get its way.

The debate about recycling the petrodollars was part of a wider debate among the main capitalist powers over whether to scrap international 'financial repression' and the system of maintaining control over international financial movements firmly in the hands of the Central Banks of states. In these debates, which took place within the IMF, the US was completely isolated, as all other governments as well as the IMF staff wanted to retain strict controls on private international financial movements.[22] But the US got its way through unilateral actions, supplementing the petrodollar move with its own abolition in 1974 of restrictions on the flow of funds into and out of the US (known, in the jargon, as the abolition of 'capital controls').

It is true that the Nixon administration was able to exploit a breach in the Bretton Woods system that had already existed since the 1950s: the international role of the City of London in financial transactions. Britain's government had allowed the City of London to operate as an 'offshore' centre for international private financial operations of all sorts almost entirely unregulated.[23] During the 1960s, the City's international business grew rapidly through the development of the so-called Eurodollar market: banks in the City accepting deposits in off-shore dollars and then lending these offshore dollars to governments and businesses throughout the world. But this role of the City as an off-shore centre was itself largely dependent upon US government policy (which allowed US banks to operate free of domestic US banking regulation by establishing operations in London).

[21] See Eric Helleiner: "Explaining the Globalization of Financial Markets: Bringing States Back in." Review of International Political Economy, 2,2 Spring 1995. This article and others by Helleiner are essential reading on the evolution of financial markets during the last quarter of a century.

[22] See Margaret De Vries: The International Monetary Fund 1972-78, Volume 1. (International Monetary Fund, Washington DC, 1985)

[23] This decision, pushed through by Harold Wilson in 1950 when he was President of the Board of Trade in the Atlee government, was undoubtedly Wilson's major contribution to the history of the world and indeed to the subsequent evolution of British capitalism.

It is worth stressing that in 'liberating' the private banks from 'international financial repression' the Nixon administration was not mainly responding to interest-group lobbying from American banks or allowing supposedly spontaneous market forces in finance to do as they pleased. The US banks themselves were initially far from happy about recycling the petrodollars to countries in the South. The US government had to lean on them to do so and had to provide incentives for such lending.[24] One such incentive was to involve the IMF/WB in new, parallel lending to such countries; another was the removal of controls on the US capital account in 1974 to enable domestic US banks to become involved in such lending so that the operations were not confined to US and other banks operating in London. A further incentive was the decision to scrap the ceiling on the amount of a bank's total lending that could go to any single borrower.[25] And finally, the US government gave its banks to understand that if they got into difficulties as a result of such lending, their government would bail them out.[26]

The Nixon strategy in 'liberating' international financial markets was based on the idea that doing so would ***liberate the American state from succumbing to its economic weaknesses and would strengthen the political power of the American state.*** According to Eric Helleiner, US officials understood in the 1970s that a liberalised international financial market would preserve the privileged global financial position of the US and grasped also that this would help preserve the dollar's central international role. Helleiner sums up the fundamental point about the overall political and economic significance of the changes: "...the basis of American hegemony was being shifted from one of direct power over other states to a more market-based or 'structural' form of power."[27]

We shall see below how these processes actually worked to strengthen the political power and economic policy freedom of the US. But first we must point out the significance of the rise of private international finance for international monetary relations between states. This rise altered the basis upon which governments maintained the international stability of their own currencies: under the old, so-called Bretton Woods system, the basis for a currency's stability was closely tied to its trade balance and to the attitude of the IMF and of the governments (Central Banks) of the main capitalist powers to the government of the country in trade balance difficulties. States with surpluses on their 'current account' (trade in goods and 'invisible' earnings, eg from profits and dividends from its companies overseas or from shares in companies overseas) had stable, strong currencies. If a state developed a current

[24] Paul Volcker later acknowledged that the recycling of petrodollars by the US banks was "accompanied by a certain amount of cheerleading by the United States government". See Gordon Smith and Fohn Cuddington (eds.): International Debt and the Developing Countries (World Bank, Washington DC,1985). The word 'cheerleading' is a euphemism for Washington's active role.

[25] See Kapstein, op.cit. Who points out that this 1979 US government decision went beyond what any of the US banks themselves had asked for.

[26] See Ethan Kapstein, op. cit.

[27] Eric Helleiner, op. cit.

account deficit, it would need to use its foreign exchange reserves to defend its currency or persuade the IMF and other governments to help.

Under the new system states with current account surpluses were still generally in a strong position. But the effective basis of their currency's stability came to depend upon another factor: the state's *creditworthiness in private international financial markets.* Under the previous system, private financial markets had been largely excluded -- banned by 'financial repression' -- from involvement in the international monetary system. Now they were to play a central role.

At first sight, these new arrangements might appear to be a liberation for governments from earlier rigidities. Even if they got into current account deficits they could borrow in the, at first London-centred, then later Anglo-American, private financial markets to tide themselves over. And they would be free to allow their currency's exchange rate to move more flexibly rather than having to subordinate all other economic objectives to maintaining a fixed rate against other main currencies. Yet the bulk of the states involved in the international capitalist economy soon discovered that the liberation was, over the longer-term an illusion. It was more like a trap.
The way the system would actually work depended on its two central mechanisms: the dollar and the increasingly American-centred international financial markets. Thus, the new international monetary arrangements gave the United States government far more influence over the international monetary and financial relations of the world than it had enjoyed under the Bretton Woods system. It could freely decide the price of the dollar. And states would become increasingly dependent upon developments in Anglo-American financial markets for managing their international monetary relations. And trends in these financial markets could be shifted by the actions (and words) of the US public authorities, in the Treasury Department and the Federal Reserve Board (the US Central Bank). Thus, Nixon gave Washington more leverage than ever at a time when American relative economic weight in the capitalist world had substantially declined and at a time when the productive systems of the advanced capitalist economies were entering a long period of stagnation.

We will call this new international monetary-financial regime the Dollar-Wall Street Regime (DWSR for short). The regime was not of course *exclusively* centred on the dollar: other currencies, particularly the mark, did acquire large roles as international currencies. And Wall Street and its large London satellite were not the exclusive sources of finance. But the Dollar-Wall Street nexus has been the dominant one by far throughout the last quarter of a century.

And it is important to note how the two poles of this system -- the Dollar and Wall Street -- have re-enforced each other. First we can see how the new centrality of the dollar turned people towards Wall Street for finance. Because the dollar has been the dominant world currency, the great majority of states would want to hold the great bulk of their foreign currency reserves in dollars, placing them within the American financial system (or in London). Similarly, because many central commodities in the world economy were priced in and traded for dollars, those trading in such commodities would wish to raise their trade finance in New York and London. Thus, the dollar's role greatly boosted the size and turnover in the Anglo-American financial markets. At the same time, there was feedback the other way. The strength of Wall Street as a financial centre, re-enforced the dominance of the dollar. For anyone wanting to borrow or lend money, the size and strength of a financial system is a very important factor. The bigger a financial market's resources and reach, the safer it is likely to be and the more competitive its rates for borrowers are likely to be. And the same is true of securities markets (for bonds or shares). For those seeking royalties from securities a big market with very high rates of buying and selling is safer because you can easily withdraw at any time by finding a buyer for your bonds or shares. Furthermore, if you are a saver looking for high returns in more risky markets it is much better to place your funds in the hands of a big, diversified operator which can absorb losses in one area of trading and compensate the losses with gains elsewhere. Thus the size and depth of the US financial markets and the growing strength of US financial operators acts as an attraction for people to place their funds at the centre of the dollar area or to raise funds in that centre. In this way, the strength of Wall Street has re-enforced the dominance of the dollar as an international currency.[28]

The Economic and Political Significance of Dollar Seigniorage

The economic and political significance of this new regime can be appreciated only when we understand the role of seigniorage in giving the American government an immensely potent political instrument in the form of the new regime.

As we saw when we initially discussed international money, a state has to acquire funds of the internationally acceptable money in order to be able to pay for goods and services from abroad. To take an extreme example, few people would accept payment from Chad in Chad's own currency: it would be useless to the overwhelming majority of people outside Chad. So Chad has to earn (or borrow) an international currency, say the dollar, from abroad before it can buy anything from abroad. But this huge constraint is non-existent for the US under the new, post-Bretton Woods international monetary regime, because the international currency is the dollar and the US does not need to earn dollars abroad: it prints them at home!

[28] This does not mean that the US commercial banks have been the biggest international banks. For much of the period the Japanese banks and some of the European banks have been bigger. But the money markets of other centres outside New York and London have been much smaller and the American investment banks have played an increasingly dominant role in providing clients with access to these pools of finance.

Seigniorage is the name for the privileges which this position gives: these can be summarised by saying that the US does not face the same balance of payments constraints that other countries face. It can spend far more abroad than it earns from abroad. Thus, it can set up expensive military bases without a foreign exchange constraint; its transnational corporations can buy up other companies abroad or engage in other forms of foreign direct investment without a payments constraint; its money-capitalists can send out large flows of funds into portfolio investments (buying securities) similarly. And as we have already seen, dollar seigniorage includes giving the US financial system great advantages as the world's main source of credit. And it is very important to appreciate the significance of seigniorage for trade relations -- imports and exports. When many of the key goods bought and sold in international markets have their trade denominated in dollars, American companies importing or exporting are far less affected by changes in the dollar exchange rate than is the case in other countries. Thus, the international grain trade does business in dollars. If the dollar exchange rate rises massively against other currencies, US exporters of grain are far less seriously affected than they would otherwise be. And if the high dollar produces a flood of imports into the United States, generating a very big, long-term deficit on the current account of its balance of payments, the deficit can be funded in dollars. Thus seigniorage gives the US government the ability to swing the price of the dollar internationally this way and that having great economic consequences for the rest of the world while the US remains cushioned from the balance of payments consequences that would apply to other states.[29]

The Economic and Political Significance of Wall Street Dominance

The Nixon administration's victory in 'liberating' the Anglo-American private banking systems for international operations had four key effects. First it suddenly catapulted private banks into the centre of international finance, pushing out the earlier dominance of the central banks and led quickly to the international dominance of the Anglo-American financial systems and American financial operators. Secondly, it opened up an enormous hole in the public supervision of international financial markets. Thirdly, it made the financial systems and exchange rates of other states, especially countries of the South increasingly vulnerable to developments in the American financial markets. And finally, it generated powerful competitive pressures within the banking systems of the OECD countries and enabled the American government largely to determine what kinds of competitive pressures and what kinds of international regulation of international financial markets should exist. It is impossible to exaggerate just how important these changes were.

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[29] These and other advantages deriving from possession of the dominant currency are known, technically, as seigniorage. For a classic discussion, see Susan Strange: Sterling and British Policy (Oxford University Press,1971). On dollar seigniorage after the destruction of Bretton Woods, see Pier Carlo Padoan: The Political Economy of International Financial Instability (Croom Helm,1986)

The first beneficiaries of the liberation of international private finance were the City of London and the big, internationally oriented US money-centre banks. In 1981 the Reagan administration enacted a law allowing so-called 'International Banking Facilities' in the US thus giving Wall Street the same offshore status as the City.[30] It might be thought that the role of the City of London suggests it should be given at least equal status with Wall Street. But this is wrong for one simple reason: the City was acting as a financial market place in dollars and its entire pattern of off-shore operations was dependent upon US government policies for international finance. It thus operated principally as a servicing centre for the dollar currency zone and as a satellite of Wall Street.

Since the early 1980s, the great bulk of the international financial market activity has thus been centred in Wall Street (and its London satellite). It is necessary to be precise about what this signifies. Frequently it is held to signify that there is a so-called 'global' financial market. This is true if it means that London and New York do business with people from all over the world. Funds flow out from and back to those two centres from and to most countries of the world. But this does ***not at all*** mean that all the financial markets of the world are unified in a single, integrated financial market. On the contrary, financial markets remained and largely remain compartmentalised not only between countries but even within countries: we can see this if we realise that even within Euroland after the launch of the Euro there will still be substantial barriers to the full integration of financial markets. But what did happen in the 1970s was that London and New York operators did begin to establish linkages between their international financial markets and national financial systems around the world which were far stronger than these had been in the 1960s. The expansion of these international private financial operations can be appreciated by comparing the size of international bank loans and bond lending between 1975 and 1990: bank loans rose from $40bn in 1975 to well over $300bn by 1990; during the same period bond lending rose almost tenfold, from $19bn to over $170bn.

Talk of a ***global*** financial market, rather than of the increasing influence of the American financial market over other national financial markets obscures the power dimension of US financial dominance. Those who believe that the adjective 'American' is trivial or even redundant should ask themselves a simple question: would they, then, be quite happy from an economic and political point of view if the international financial system was dominated by the markets and operators of China or Iraq, just so long as they could offer similar kinds of credit or other financial services on similar terms to those of Wall Street? But to make the point much more directly, we can simply note that because the American financial markets have been dominant within the hierarchical networks of financial markets, access to that market, different kinds of linkages between national economies and that market and price movements in that market have enormous economic ***and political*** significance.

The story since the 1970s has been one of growing pressures from the Wall Street centre to weaken the barriers to its penetration into domestic financial systems. This pressure has a triple target: first to remove barriers to the free flow of funds both ways between Wall Street and private operators within the target state; second to give full rights to Wall Street operators to do business within the financial systems and economies of the target states; and

[30] See Jerry Coakley and Laurence Harris: The City of Capital. (Blackwell,1983)

thirdly, to redesign the financial systems of target states to fit in with the business strategies of Wall Street operators and of their American clients (transnational corporations, money market mutual funds, etc.)

Of course, Wall Street and London have not had a monopoly. Tokyo has grown and some of the biggest financial operators are Japanese. Frankfurt, Zurich, Paris, Hong Kong and Singapore are all important. But none of these other centres as yet comes close to rivalling the size of Wall Street and London and in financial affairs even more than in any other sector of business, market size and the size of the funds operators can mobilise is *competitively decisive*.[31] You can do what smaller players can't, so you can set the pace of most of the innovations in the field.

This competitive advantage was multiplied by the almost entirely unregulated nature of the London and Wall Street centres. Such regulation as existed amounted only to rather vague, non-legal guidelines agreed by central banks in the Bank for International Settlements.[32] This, together with scale advantages, not only maintained Wall Street's dominance but started a corrosive process of undermining the public regulation of financial operators *within* other states, as operators there escaped off-shore themselves to compete, found ways around local rules and exerted pressures on their governments to liberalise in order to enable them to compete against Wall Street.

As we saw above, it is dangerous for banking systems if banks' operations are allowed to go unregulated. Unbridled competition between banks leads them to compete with each other to the point of collapse. But because of the dominance of Wall Street in private international finance, what competition, what regulation and what international arrangements for banks becoming insolvent should be established became questions largely in the hands of the American government, in alliance with the British authorities. If the US government chose not to regulate, it became extremely difficult for the other main capitalist states to maintain their regulatory frameworks. If the US decided to regulate, other banking authorities would follow suit, but the US could still largely dictate the form and scope of regulation. Thus a whole chain-reaction of effects and pressures on banking systems around the world was unleashed by the decisions taken in Washington.

Let us mention some of these chain reactions. First, the US Federal Reserve could largely dictate the levels of international interest rates through moving US domestic interest rates. It could thus determine the costs of credit internationally, with enormously powerful effects on other economies. When international private credit is cheap economic operators with access

[31] See Eric Helleiner: "The Challenge from the East: Japan's Financial Rise and the Changing Global Order" in P.G.Cerny (ed.): Finance and World Politics: Markets, Regimes and States in the Post-Hegemonic Era (Edward Elgar, 1993).

[32] The so-called Basle Committee of the BIS drew up a 'concordat' among central banks in December 1975 which was revised in 1983 and again in 1991. It was a gentleman's agreement, which failed to establish clearly 'lender-of-last-resort' responsibilities, supervision of banks' overseas subsidiaries and agencies, reserve requirements and measures for combatting fraud.

to cheap international credit start projects which seem viable in the current conditions. But if US decisions suddenly make credit very expensive, fundamentally sound enterprises may find themselves going bankrupt because of a sudden contraction of cheap credit. And an international financial system dominated by the US financial market can swing wildly, oversupplying credit at one moment and dramatically contracting it at another. To make matters worse, the tempo of the US business cycle is impossible to predict with accuracy and the direction of US policy is equally impossible to predict because the US has qualitatively greater freedom of policy choice as a result of its dominant political position in the international economy.

Secondly, through its regulatory interventions or the lack of them, Washington was the manager of what might be called the micro-economics of international finance: it could dictate how much regulation and supervision of bank lending there would be. De facto it managed the international tension between encouraging the banks to take risks and preventing them from acting recklessly and then collapsing. Frequently during the last quarter of a century, Washington has been happy to forget about regulating its international financial operators, whether, as in the 1970s there are the big US money-centre commercial banks or whether they are the investment banks or the hedge funds of the 1990s. When this happens, enormous competitive pressures are placed upon financial operators elsewhere, and they pressurise their governments to relax their regulations, or find ways of evading what regulations exist. The cry is often heard in Washington that for technological or other reasons regulation is impossible. But when it suits Washington to introduce regulation it has been shown to have been able to achieve it, with remarkable ease.

This was shown with the so-called Basle Accord of 1988 laying down guidelines for international banking supervision. The Basle Accord was achieved through the US government forming an alliance with London for a joint Anglo-American regulatory regime. This was enough to ensure that all other OECD governments would come together to establish a common regime. The resulting regime has been a ‘gentleman’s agreement’. And the result of the accord was a regulatory regime skewed towards serving US interests since it gives all banks an incentive to privilege the buying of government bonds, a pressing US need, given its government’s indebtedness, and a disincentive to lend to industry. This Accord demonstrated just how easy it is for states to regulate international financial markets, on one condition: that the regulation is done with US support.[33]

Thirdly and very importantly, US governments discovered a way of combining unregulated international banking and financial markets with minimal risk of the US banking and financial systems suffering a resulting collapse. Using its control over the IMF/WB and largely with the support of its European partners, Washington discovered that when its international financial operators reached the point of insolvency through their international operations, they could be bailed out by the populations of the borrower countries at almost no significant cost to the US economy. This solution was first hit upon during the Latin American international financial crisis at the start of the 1980s and it was a solution with really major economic and political significance. We will return to this experience later.

[33] For further details of the Basle Accord, see Kapstein, op. cit.

At the same time, the US government developed ways of extending the influence of Wall Street over international finance without putting its big commercial banks at risk. It successfully sought to change the form of lending to the more rentier-friendly bond market and towards more short-term lending rather than medium or long term bank loans.

The final and most important area in which Wall Street dominance over international finance has political significance lies in the fact that financial systems are both enormously important parts of any capitalist system and they are at the same time interwoven with core control functions of capitalist states. It is through its control over financial flows that capitalist states exercise much of their political power over society. Insofar as Wall Street could strengthen its linkages with national financial systems, breaking down state barriers to the thickening of linkages with domestic financial systems, these latter would tend to slip out of the control of their domestic states. In a crisis within a national financial system, the American state itself could open the whole capitalist system of the state concerned to being re-engineered in the interests of American capitalism.[34]

The US and Global Management

Just as the state plays a central role in domestic monetary and financial affairs, whether the domestic regime is Keynesian in structure or neo-liberal, so the main states or state play a central role in international monetary and financial affairs. The fact that these continual political interventions in these central aspects of the international economy tend not to register in much of the literature on international economics is the result of ideological blinkers, all the more powerful for being entrenched in the professional academic division of labour between political science and economics. These blinkers are evident in those definitions of globalization which suggest it is a purely techno-economic force not only separate from state-political controls but inimical to them.

But these blinkers are re-enforced also by the fact that state political influence over the international monetary and financial system is not neatly parcelled out between states. To put it mildly, political influence in these areas is distributed *asymmetrically: during the last quarter of a century it has been distributed overwhelmingly to one single state.* Under the Bretton Woods regime, there was something like a global authority, resting on the co-operative agreements laid down in the 1940s: gold functioned as a supranational monetary anchor, the IMF and Central Banks sought to manage monetary and financial flows. Of course, the US was overwhelmingly the most influential player within this IMF system. But it too was constrained in what it could do by the supranational rules of the system. The central point about the new, post-Nixon regime was that the US was still overwhelmingly dominant but not it was not constrained by rules. The Dollar-Wall Street Regime has been a bit like the British constitution: the dominant power has been able to make up the rules as it went along. The US could decide the Dollar price and it could also have the deciding influence on the

[34] On the centrality of financial systems for state power, see Jeffrey Winters: “Power and the Control of Capital”, World Politics, 46, Winter 1994. See also Sylvia Maxfield, Governing Capital. International Finance and Mexican Politics (Cornell University Press, 1990); and Jung-en Woo: Race to the Swift: State and Finance in Korean Industrialisation (Columbia University press, 1991)

evolving dynamics of international financial relations.

So we arrive at a question of absolutely cardinal importance both economically ***and politically***: would the US government run the new Dollar-Wall Street Regime in the American national interest? Or would the United States government rise above mere national interest and pretend it was a supranational world government subordinating all national interests including those of the USA to the collective global interest? Or would the US government steer a middle course and set up a collegiate board of the main capitalist states in a more or less large (or small) oligarchy in which the US would compromise its national interest to some extent for the collective good of the oligarchy?

The answer is that the United States government has done its constitutional duty. It has put America first. The whole point of the Nixon moves to destroy the Bretton Woods system and set up the Dollar-Wall Street regime ***was to put American first.***

There is a straightforward test that can be applied to detect the direction in which US policy has been applied. Has the US sought to establish rules and instruments for the effective public management of international money and international finance within the DWSR of the kind shown to be necessary in domestic economic management? We can run through the check-list of issues:

1. There is a very strong international interest in international monetary stability. Yet instead, the DWSR has seen the price of the main international currency has been driven up and down in wild swings without historical precedent, swings that make even the 1930s look like an era of relative monetary calm! This extraordinary volatility has been the product of deliberate US policy and of Washington's refusal to work towards a stable, rule-based system.
2. Public macro-regulation of the supply of credit within the world economy to ensure some measure of stability: instead international flows of credit have swung wildly from over-supply to chaotic contraction in cycle after cycle, again overwhelmingly because Washington has wished matters to be handled in this way.
3. Public micro-regulation of the main private credit suppliers to try to ensure minimally responsible behaviour, to try to restrict dangerous competitive pressures and prevent major collapses in either the financial sector or productive sector: instead of this there has been a free-for-all in this area, except insofar as the American government has wished to impose such regulation.
4. Public management of the interface between finance and the productive sector internationally to provide incentives for channelling funds into productive activity, rather than speculation, insider trading, market rigging and corruption: The record in this area speaks for itself: there has been a systematic drive to make state after state subordinate its management of productive activity to the unregulated dominance of international finance and to make all states increasingly powerless to resist such dominance (again using the IMF and the World Bank as central instruments against the role of public authorities in this area).

A number of authors have suggested that the subsequent history of US international monetary and financial policy has been bound by the rules of co-operative oligarchy with the rest of the G7. But the evidence for this is extremely weak as regards the main strategic lines of US policy. The existence of the G7 proves nothing except that the US has sought to use it to get the other main capitalist powers to do what the US has wanted. The fact that on many occasions other G7 countries have not been prepared to do the US's bidding does not mean the US itself has adopted a collegiate approach. Some authors have pointed to the supposedly great significance of the 1978 Bonn summit as an instance of co-operative policy-making.[35] It was, but in the form of Germany's government agreeing to do most of what the US government wanted. And whatever co-operative spirit there was in the Carter administration vanished under Reagan.[36] The strongest claim for collegiality in high monetary politics concerns the Plaza Accord to lower the dollar price in 1985. It is quite true that this meeting did agree to bring down the dollar and it subsequently was brought down. But as Destler and Randall Henning show, US Treasury Secretary Baker had already decided to bring down the dollar had already started to bring it down and was interested in using the G7 agreement as a tactical ploy within US domestic politics against those who were opposing his already decided policy for a fall in the dollar.[37]

And in the management of international finance, the America First policy has been equally evident. During the 1970s, the US governments first treated the IMF with contempt (under Nixon), then allowed it to sink towards oblivion (in the late 1970s). What discussions on the regulation of international finance did take place shifted to the Bank for International Settlements and to bilateral discussions. The Reagan administration was at first downright hostile (and vitriolically hostile to the World Bank). It changed its tune towards these organisations not out of any abandonment of America First unilateralism, but because Baker saw, during the Latin American debt crisis just what extraordinarily valuable tools of American economic statecraft these two institutions could be, once their new, subordinate roles were defined. Oligarchic collegiality had nothing to do with the matter. The record is one of US administrations seeking to be extremely collegial, provided the co-operation is about working together along the lines of action laid down in Washington already.

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[35] Richard N Cooper, Robert Putnam, Barry Eichengreen, C.Randall Henning and Gerald Holtham: Can Nations Agree? Issues in International Co-operation (The Brookings Institution, 1989)

[36] See Robert D.Putnam and Nicholas Bayne: Hanging Together. The Seven-Power Summits (Heinemann, RIIA, 1984) They argue that the summits were useful, but make no claim for co-operation on international monetary policy.

[37] I.M.Destler and C.Randall Henning: Dollar Politics: Exchange Rate Policy-making in the United States. (Institute for International Economics (Washington DC, 1989)

A whole academic paradigm has been constructed in the United States to justify this American unilateralism. This explains that there can be stability in international monetary affairs only when one single power is overwhelmingly dominant (hegemonic). The theory goes on to explain the turbulence: it is because the US is no longer totally dominant. The theory has been intellectually demolished.[38] But it at least has the merit of trying to explain the extraordinary behaviour of US governments in the management of international monetary affairs over the last quarter of a century.

This, then, brings us to a final question: if US policy over international monetary and financial affairs has been government by the US national interest, does this mean the perceived national economic interest or the national political interest or both? To prove a satisfactory answer to this question we need to have a theory of what the economic and political interests of capitalist states at the top of the international hierarchy of capitalist states actually are. This in turn requires a grasp of the dynamic internationalising drives within capitalism itself. We will not address these questions until later. Instead, we will simply restrict ourselves to the propositions which we have sought to demonstrate so far: first that a new international regime for money and financial relations was created in the 1970s. Secondly, that the dynamics of this regime were inescapably and integrally tied to the behaviour of one state in the inter-state system (the USA) and of one financial market in the networks of international finance ('Wall Street'). And thirdly, that US administrations followed their constitutional duties in approaching their management of this regime from a National Interest perspective.

The DWSR as a self-sustaining regime.

We are now in a position to notice the pattern of functioning of the DWSR. The dollar is the international money to which all other convertible currencies are linked by exchange rates. The American government chooses not to seek fixed exchange rates with the other main currencies, since that would require the US government to give up its use of the dollar price as an instrument for achieving other goals. Therefore, under the regime, the dollar moves in great gyrations up and down against the other currencies, utterly transforming their trading and other environments. And within these macro-swings there is constant micro-volatility. States and economic operators around the world must structurally adapt their operations to this constant macro and micro volatility of the dollar or risk various kinds of domestic economic imbalance or crisis.

At the same time the American-dominated international financial market and its private financial operators inter-act to an ever-greater extent with the international monetary relations of the dollar system. The dollar's dominance as the international currency means that states build up foreign exchange reserves mainly in dollars. Exchange rate turbulence means that states wishing to try to maintain the stability of their own currency need larger reserves than before. These reserves are placed in the US financial markets (such as US Treasury bonds) because their liquidity means the funds can easily be withdrawn for exchange rate stabilisation purposes. At the same time, Wall Street offers the most competitive terms for governments wishing to borrow money for various purposes (including

[38] See Andrew Walter: World Power and World Money (Harvester Wheatsheaf, 1993)

defending their currencies) and it offers new instruments so that governments and economic operators can tackle problems of exchange rate turbulence: not only a vastly expanding foreign exchange market but a whole new range of so-called derivative markets such as forward foreign exchange derivatives, swaps of currencies, loans etc. Although many attribute these innovations to ‘technology’, they are simply a creative response to enormous turbulence in the currency markets: the forward foreign exchange markets and interest rate swaps markets, for example, enable operators to hedge against the risk of future shifts in currency prices.

Much of the globalization literature which seeks to persuade us of the unstoppable, crushing strength of ‘international capital markets’ refers us to the huge size of the foreign exchange derivatives markets, the huge volumes of currencies traded in the foreign exchange markets or the extraordinarily rapid turnover in the US Treasury bond markets. Yet these volumes are overwhelmingly the result of politically-driven volatility in international monetary relations.

To cope with their volatile environment, governments borrow from the private financial markets, but such borrowings are typically themselves subject to volatile repayment terms (by being linked to movements in US short-term interest rates) and furthermore they are borrowing in dollars and since the dollar swings wildly, the value of their debts (in terms of real domestic resource claims) will vary with their exchange rates with the dollar. Thus the links with Wall Street subject borrowers to further turbulence.

The international dynamics of the regime then interact with domestic economic management on the part of individual governments. Sudden swings in the dollar produce sudden swings in a state’s trade balance and terms of trade. The government faces a choice: use Wall Street borrowing as a cushion, or engage in domestic macro-economic adjustment. Ease of the latter choice depends on the domestic socio-political strength of the government: can it easily balance its budget and right a trade deficit by imposing costs on various domestic social groups or not? If this is difficult, the government may choose to borrow dollars from Wall Street. When Wall Street is flush with inflowing funds, it is eager, if not desperate to lend and offers governments inducements to borrow. But this may only cause a greater adjustment problem down the road, a problem which can strike suddenly through a further shift in the dollar or in US interest rates (or Treasury bond rates).

These dilemmas are faced particularly acutely by economies weakly inserted in international product markets, with weak economies and adjustment problems which the governments are too weak socio-politically to manage. These problems are, of course especially prevalent in countries of the South. Thus the regime systematically generates payments and financial crises in the South. Every year one country after another suffers financial crises. As the Wall Street economist Henry Kaufman points out, national financial crises “have come repeatedly on the international side in the last 20 years.”[39] An internationally provoked crisis then provides the role of the IMF/WB in the regime as auxiliary players. If such financial

[39] Henry Kaufman,”Fundamental Precepts Guiding Future Financial Regulation”, address to the International Organisation of Securities Commissions, London, 27th October,1992, cited in Epstein, op. cit.

breakdowns were not a systematic element in the regime, the IMF's role would have been marginal, if not redundant. Their task is to ensure that the state concerned adjusts domestically so that it can maintain the servicing of its Wall Street debts. At the same time the IMF acts internationally in the way that a domestic state acts when its central financial operators get into trouble: it bails them out. But there is a crucial difference in the international field. When an American bank gets into trouble in the American domestic economy the US tax-payer bails it out. But when the same American bank gets into trouble abroad, the bailout is paid for not by the American tax-payer but by the population of the borrowing country. Thus the bank's risk is borne by the people of the borrower country, via the IMF's auspices.

Through IMF/WB intervention the state in crisis is eventually able to re-integrate into the DWSR, but this time with heavy debt-servicing problems and usually with a weakened domestic financial and economic structure. Meanwhile the external environment is as volatile as ever and the state concerned is more likely than not to face a further financial blow-out in the not too distant future.

But one of the paradoxes of the DWSR is that such financial crises in the South do not weaken the regime: they actually strengthen it. In the first place, in the crises, funds tend to flee from private wealth holders in the state concerned into Wall Street, thus deepening and strengthening the Wall Street pole. Thus during the debt crises of the early 1980s in Latin America, the following very large outflows of funds occurred: from Argentina, $15.3Bn; from Mexico $32.7bn, from Venezuela, $10.8Bn.[40] Secondly, to pay off its now higher debts the state concerned must export into the dollar area to find the resources for debt servicing. This further strengthens the centrality of the dollar. Thirdly, the risks faced by US financial operators are widely covered by the IMF, enabling them to return to international activity more aggressively than ever. Finally the weakening of the states of the South strengthens the bargaining power of the Wall Street credit institutions in decisions on the form of future financing. Forms which are safer for the creditor money capitalist are increasingly adopted: securitised debt and short-term loans rather than long-term loans. And so on and so on.

Through all the gyrations of American policies for the world economy, the DWSR has remained firmly in place, constantly reproducing itself. In 1995 the dollar still remained overwhelmingly the dominant world currency: it comprised 61.5% of all central bank foreign exchange reserves; it was the currency in which 76.8% of all international bank loans were denominated, in which 39.5% of all international bond issues were denominated, and 44.3% of all Eurocurrency deposits; the dollar also served as the invoicing currency for 47.6% of world trade and was one of the two currencies in 83% of all foreign exchange transactions. And if intra-European transactions were eliminated from these figures, the dollar's dominance over all other transactions in the categories listed above becomes overwhelming.[41]

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[40] See Mohsin S.Khan and Nadeem Ul Haque: "Capital Flight from Developing Countries", Finance and Development, 24,4, March 1987.

[41] See statement by C. Randall Henning before the US Senate Committee on the Budget, 21st October,1997.

The DWSR and the Conventional Notion of Regimes

The notion that there are regimes in international relations was first put forward in the 1970s by Robert Keohane and Joseph Nye,[42] and was given its classic definition by Stephen Krasner in 1983.[43] Krasner defined regimes as 'principles, norms, rules and decision-making procedures around which actor expectations converge in a given issue area'. This concept has become extremely influential in the analysis of international relations and in the functioning of multi-lateral organisations. The notion of regime which is used here overlaps in some respects with Krasner's notion but differs with it in certain fundamental respects.

The DWSR is a regime in Krasner's sense in three respects. First, it corresponds to the idea that international relations do not consist simply of states inter-acting with each other in an anarchic void alongside economic operators interacting with each other as atoms in a world market. There are patterned, structured regimes governing these interactions. The DWSR is a regime in this sense of an international mechanism which structures and patterns interactions. Secondly, the DWSR corresponds to the idea implicit in Krasner's notion, that the states participating in these regimes do so because they find it in their interest to co-operate in the regime. This is true also of the DWSR. Thirdly, Krasner is prepared to accept that one state, the dominant state, is often the decisive and even unilateral actor in establishing the regime: it is not to be imagined that it is established consensually or in a collegial fashion. This imposed character of a regime can apply also to the DWSR.

But here the agreement ends. Krasner conceives of his regimes as being quasi-legal in character. States have, in his view, come to adopt a set of rules or norms or principles or a fixed set of collective decision-making procedures. Yet dollar dominance and the governing of international currency prices by the dollar exchange rate is not a quasi-legal norm or rule: it is *a fact* which regularly reproduces itself. All states that maintain any degree of currency convertibility *participate in this fact*: the price of their currency will be fixed, directly or indirectly in relation to the dollar. States do have the option of exit from the regime: they can make their currency inconvertible. But if they do they will tend to be excluded from significant participation in the world economy. And the fact that states do participate in the regime does not indicate that they find it beneficial: it simply indicates that they lack the power to do anything about it.

The same applies to the other pole of the regime: the American financial market. States and economic operators do not have to participate in this market. They can avoid placing their reserves there, they can avoid borrowing there, but in practice it is almost impossible for them to avoid being drawn in because of their need for finance for their economic activities as a whole. And if they need to borrow from abroad, the most economically rational source of borrowing is from the biggest most competitive/unregulated and most liquid markets -- Wall Street.

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[42] See R. Keohane and J. Nye: Power and Interdependence (Little, Brown &Co.1977)

[43] S.D.Krasner: International Regimes (Cornell University Press,1983)

There is another problem with the Krasner definition. Its attempts to present regimes as operating within discreet 'issue areas'. The DWSR does not occupy an ' issue area': it occupies a position as the monetary and financial framework facing states in their attempts to come to grips with a vast range of issue areas in international and domestic politics and economics. And the attempt to confine regimes to 'issue areas' chops reality up in trivialising ways: there is no equivalence of kind between an international legal regime for ensuring air safety and a framework regime like the DWSR. A further problem lies in the fact that regime theorists will tend to treat institutions like the IMF/WB as Krasner-type regimes, divorcing them from the patterned regularities of the DWSR in which they operate and which gives meaning to the dynamics of the IMF/WB's activities. And a final problem with the Krasner definition of regimes is that it presupposes a separation between regimes on the one side and both states and markets. Yet the DWSR includes as integral parts of its structures both states and markets.

PART THREE: THE EVOLUTION OF THE DWSR FROM THE 1970S TO THE 1990S

A.The US Policy for the Evolution of the DWSR From Nixon to 1993

After Nixon the story of US administrations and the DWSR is a mixture of two strands: first, an extraordinary series of gambles both with the dollar and with international private finance, in both cases exploiting the regime; and second, a growing belief in the central importance of the DWSR for US international interests and attempts to deepen the DWSR and radicalise it. These two themes both involved an approach of 'America first', but there was no consistent master plan until the 1990s and the Clinton administration. Rather, a strategic view of the regime's role in a US national strategy emerged gradually, often in the midst of crises caused by earlier gambles going wrong. At every stage, American administrations managed to expel the costs of these blunders outwards onto others and throw themselves into new tactics which had the effect of deepening the regime. Only in the 1990s, and especially under the Clinton administration, did a consensus seem to emerge within the American capitalist class that maybe at last they had discovered a master plan, comprehensive in scope and with all the tactical instruments for its ultimate complete success. But this too, in the form pursued by the Clinton administration may also turn out to be another blundering gamble. Each phase of this story does not end with the world back where it started. Instead it is marked by a constant evolution of the inner logic of a DWSR exploited in American interests

The Carter administration was attempting to use a low dollar to maintain some sort of growth strategy centred on the industrial sector and on traditional quasi-Keynesian techniques. Between 1975 and 1979 the dollar lost over a quarter of its value against the Yen and the Mark as the Carter administration sought to boost output and exports of the US manufacturing sector. At the same time, apart from its interest in using the flexible dollar-price for industrial policy, the Carter administration was indifferent to the potentialities of developing or exploiting the DWSR.

Matters changed only with the Reagan administration. The turn in dollar policy had begun before Reagan's election. Worried that the dollar's fall might slip out of control and worried about rising inflation combined with industrial overcapacity, Federal Reserve Chairman Volcker made his famous turn, jacking up interest rates, swinging towards a strong dollar and a drive to restore money's role as a stable standard of value (rather than just as an inflationary means of circulation). These steps were taken much further by the Reagan administration.

The central features of the Reaganite turn in matters of political economy were twofold: first, to put money-capital in the policy saddle for the first time in decades; and secondly to extend and exploit the DWSR in the interests of America first. Putting money capital in the saddle involved squeezing out inflation (which eroded royalties on money capital), taking steps to deregulate the banking and financial sector, offering huge tax cuts for the rich which always boost the financial sector and rentier activity and pursuing a high dollar policy. Industrial growth would be driven principally by a great expansion of the defence budget, running an expanding budget deficit and sucking in capital from abroad. This aspect of policy essentially meant that the US state was acting as a surrogate export market for the industrial sector. The new dominance of money capital and the anti-inflation drive was essentially an incentive to employers of capital to begin an assault on the power, rights and security of their workers to restore profitability.

But Reagan's team also began to seek to deepen the DWSR, initially as a pragmatic set of solutions to discreet problems. Thus, maintaining a very high dollar could have meant chokingly high US domestic interest rates unless the US government could attract very large inward flows of funds into US financial markets. To achieve such flows, it began a drive to get rid of capital controls in other OECD countries, especially Japan and Western Europe. Thus began a long campaign to dismantle capital controls.

The first decision of the Thatcher administration on coming into office in 1979 had been to end British controls over financial movements. Holland followed in 1981 and Chancellor Kohl swiftly did the same in 1982 on coming into office. A major breakthrough for the campaign came with the French government's decision in 1984 to promote the idea of the European Single Market: this was above all a decision to remove controls on financial movements throughout Western Europe. Denmark liberalised in 1988, Italy started a phased liberalisation in the same year and France started phasing out capital controls in 1989[44]. During the 1980s, the US pressured the Japanese government with some success to liberalise its restrictions on the free exit and entry of funds. This was a major step in boosting the size and weight of the Anglo-American financial markets.

At the same time, the turn to the high dollar/high interest rates posture from the Volcker shift in 1979 set the stage for the Latin American and East Central European debt crises of the early 1980s. Volcker did not raise interest rates and support a high dollar in order to produce this crisis. It nearly produced a collapse in the US banking system, but in the course of managing the crisis, the Reaganites, who were very interested in bringing Third World capitalisms to heel, learned some very powerful lessons. They learned an old truth from the days of European imperialism: the imperial power could take advantage of a country's debt crisis to reorganise its internal social relations of production in such as way as to favour the penetration of its own capitals into that country. Thus started the use of the DWSR to open countries's domestic financial regimes and domestic product markets to American operators.

[44] Ruth Kelly: Derivatives -- a Growing Threat to the International Financial System in J.Mitchie and J. Grieve Smith(eds.):Managing the Global Economy (OUP,1995)

The second lesson, learnt by American financial operators, was that the kinds of long or medium-term syndicated bank loans used for recycling the petrodollars was too rigid since it locked the funds of these banks up in the fates of the borrowing countries. Therefore they sought to shift towards much safer operations with interest-bearing capital: lending through bonds from which they could withdraw by trading them on the securities markets. They also learnt that they could get crisis-ridden target countries to build domestic stock markets and could start to play these as a profitable way to earn royalties. But these kinds of operations would require removing the controls on the capital accounts of such countries. Yet another fundamental lesson from the Latin American crisis was a very important paradox: financial crisis in a country of the South could actually boost Wall Street through capital flight. When a financial crisis hit a country, large funds would flee not only that country but others fearing contagion and the funds would flee to the Anglo-American financial nexus, boosting liquidity, lowering interest rates and having a generally healthy impact.
And the final, and in some ways most important lesson was that the IMF/World Bank were not, after all, a waste of time for American capitalism. With the establishment of the DWSR, the IMF was elbowed out of the way by the US Treasury and the US financial markets and seemed headed for history's proverbial dustbin. Reagan came in with no intention of reviving it. As for the World Bank, the Reaganites viewed it as a semi-subversive institution, saturated with old-style quasi-Keynesian 1950s US 'development' nonsense. But Reagan's Treasury Secretary, James Baker, learnt in the debt crisis just what a powerful tool these bodies could be as facade-cosmopolitan agencies for advancing the interests of American capitalism. Thus from the unveiling of the so-called Baker Plan for generalised 'Structural Adjustment' in Seoul in 1985 the IMF/WB found themselves with new international roles.

It is important to note how they have served above all US interests: they have not done so mainly through conspiratorial manipulation (which does not mean, of course, that there were no conspiracies -- there were no doubt lots -- hence the extraordinary veil of secrecy surrounding their decision-making). Instead their role has rested on two mechanisms: first by defending the integrity of the international financial system the IMF was defending a system of US exploitation of the DWSR. Second, by restructuring domestic economies to enable them to pay off their debts, the WB was adapting them to the same US-centred international system: the necessities of its structure pushed them towards domestic deflation, currency devaluation and an export drive along with measures to ease budget deficits and earn foreign currency on the capital account by privatising with the help of foreign capital and attracting inward flows of hard-currency funds through liberalising the capital account. Thus did US rentiers get their debts paid, US industry got cheaper imports of the inputs needed for production, US companies could buy up assets including privatised utilities in the country concerned, and the capital account would be liberalised so that local stock markets could be played. And the whole system could be made even more rule-based by the fact that neo-classical economics supplies us with hundreds of rules and norms and almost all of them are never quite operating in any country at any time. So the IMF and WB could simply pick and choose whichever aspect of a domestic economy they wanted to concentrate change upon and could always point to some rule or norm of neoclassical economics that was not being met!

Just as the Nixon-Ford-Carter phase left a hang-over for the Reaganites, so the Reagan period left a hangover for Bush: this time the huge double deficits on the balance of payments and the deficit and no money in the kitty for exerting influence over the Soviet Bloc region as it collapsed, especially because of the domestic speculative blow-out in the housing sector of the financial system. But the dialectics of progress through blundering gambles continued to work since the debt crisis had produced a development of the DWSR which could be exploited by the US to overcome its weaknesses in its efforts to dominate developments in Russia and Eastern Europe. The IMF-Structural Adjustment sub-system could be imposed upon the region with the claim that it was the new global development paradigm and not an ad hoc device for serving US interests in the Latin American crisis. Bush showed great skill in persuading the West Europeans to knuckle under to IMF (US Treasury) leadership over the transition in the East and the result was to perpetuate and strengthen the reach of the DWSR, giving great scope for US financial operators to link up with the ex- nomenklaturas of the region in orgies of speculative, corrupt and extremely profitable ventures, through privatisations, through using local stock markets as playthings in the hands of US investment banks, through using dollars to buy huge quantities of assets in Russia and elsewhere, through earning extraordinarily high yields on East European government debt in the bond markets, through enormous injections of (largely criminal) East European flight capital into the Anglo-American markets and through, at every turn, taking large, juicy fees for services rendered. It was, all in all a remarkable success story, especially given the fact that the catastrophic costs of the whole enterprise lie in far away Eastern Europe as a problem which the West Europeans have to try to contain, no doubt with the help of NATO.

At the time that Clinton became President in 1993 the DWSR had thus sustained itself for a full twenty years. The dollar was still the overwhelmingly dominant international currency and the weight of Wall Street in the international economy was far greater than it had been in the 1970s. The various kinds of boundaries which had existed between national financial and economic systems and the Wall Street-centred international financial markets had been eroded and in some countries almost entirely swept away. And the linkages between countries in the former Eastern Bloc and the South with Wall Street had been greatly strengthened through debt dependence, while the form of that debt dependence was changing from one based upon long or medium-term bank loans to one based upon debt securities or short-term loans -- a form of dependence far more vulnerable to short-term movements in the Wall Street securities markets. Alongside these developments the other main feature of the regime's evolution was the increasingly important role of the IMF as a public authority for managing the effects of the regime on countries of the South and former Eastern Bloc. The IMF was not acting as a public authority *above all states* but as a public authority for transmitting the policy of the states controlling it -- which meant, above all the USA --into the states in varying degrees of crisis as a result of the regime's operations.

During the Clinton administration, as we shall see, there would be a drive to radicalise the DWSR both to sweep away the barriers between the Wall Street-centred international financial markets and nation states and to impose a new set of restrictions on the domestic actions of nation states. There would also be a dramatic attempt to radicalise the way the US government used the DWSR for the purposes of national economic statecraft. But before examining the Clinton period we will briefly survey the impact of the DWSR on the rest of the international political economy during the period from the 1970s to the early 1990s.

B.The Responses of Political Economies to the DWSR

Up to now we have concentrated only upon the role of the US in the DWSR. But we must briefly survey the responses of the other main components of the world economy to this system since its launch in the 1970s.

During the post-war period, the core of the world economy was made up of a German-centred Western Europe and Japan, along with North America. The revival of the capitalisms at the two opposite ends of Eurasia had followed very different patterns from the angle of international political economy. Germany's revival was built upon the development of deepening regional links within Western Europe. Japan's revival took place largely in regional isolation and through deepening links with first the American and then also with the West European markets. Thus the move towards the dollar-Wall Street system in the 1970s had very different impacts upon these two non-American centres, as we shall see. Neither the leaders of German capitalism nor those of Japan welcomed or approved of either the inauguration or the evolution of the DWSR nor of the various ways is which the US has sought to exploit it. On the other hand, in both regions the DWSR regime has had its supporters and even enthusiasts, especially, of course, in countries like Britain and Holland with powerful financial sectors and amongst those most closely involved with private international finance.

Germany and Western Europe

Both Western Europe and Japan were, of course, extremely hostile to and worried by the international monetary chaos inaugurated by the DWSR in the early 1970s. The West European responses developed along four axes. First a defensive response to the regime in the monetary field by building a new regional monetary regime in Western Europe: the exchange rate mechanism, leading towards a full monetary union. Secondly, a shift towards a new accumulation strategy which placed money capital in dominance over employers of capital. Thirdly, an attempt to exploit the DWSR internationally; and fourthly, an intra-European conflict over the role of rentier capitalism within Western European society. We will look at each of these strands in turn.

1. The regional monetary regime: without of defensive regional response to the DWSR the development of the European Community towards a customs union would have been destroyed by chaotic intra-European currency movements which would have made a mockery of intra-European free trade. So Germany was able to persuade its main West European partners to manage their currencies under Deutschmark leadership. In this way, monetary stability could be maintained within Western Europe. The Mark would be the point of contact between the West European economy and the wild dollar. And German governments in the 1970s were prepared to claim that their leadership would be just a phase on the road to full monetary union (as the French wanted). Despite a very shaky start in the 1970s and various crises in the 1980s and 1990s, this system has held.

The Soviet Bloc collapse raised uncertainty about this system, through raising uncertainty about the future direction of German capitalism. Chancellor Kohl responded with the decision to maintain the regional arrangements by deepening them into full monetary union. This decision has held.[45]

[45] The spontaneous rationality for German capitalism would have required a smaller Mark union, without the Mediterranean countries, and with an eastward orientation. But Germany was pushed politically into the big EU monetary union, something which will

require a major adjustment either by Germany (financial transfers) or by the Mediterranean countries.

2. Free financial flows and the new centrality of money-capital: A number of West European states sought to maintain the Keynesian mode of accumulation in which industrial capital's expansion was the central target of policy. The French Socialist government attempted this in the early 1980s. This effort was frustrated not least because of the Reagan administration's economic statecraft. It used the high dollar and high interest rates as a weapon against the French project .[46] The failure of the French project led the Mitterrand government to accept the scrapping of controls on international financial movements as part of a wider strategy (the single market and the achievement of monetary union). With a policy framework consisting of fixed exchange rates and free movement of finance, West European governments except Germany's lost most of their control over monetary policy to the private financial markets of Europe.[47] When European governments declared that 'globalization' had meant that they had lost the ability to steer their domestic economies as before, they actually meant that their determination to subordinate domestic economic management to fixed European exchange rates and free movement of finance was what was tying their hands domestically. This shift brought about a similarity in domestic macroeconomic priorities between Western Europe and the USA: the priority of low inflation, maintaining money's role as a fixed standard of value in the interests of money capital and pushing employers of capital to engage in labour shedding activity and downward pressure on wage costs.

3. The attempt to exploit the DWSR internationally: At the same time, West European capital, faced with domestic long-term stagnation over the last quarter of a century, was able to exploit the possibilities offered by the DWSR regime to turn outwards beyond the core in search of new fields of accumulation. It was thus able to live with and benefit from the use of this regime to open economies elsewhere, and to live with US leadership of the regime.

4. The conflict over the role of the rentier sector: Although the power of money capital within the balance of money-capitalists/employers of capital was sharply shifted by the changes described above, most governments in Western Europe did not go along with the idea of dismantling the entire institutional framework for controlling their financial systems and their inter-faces with the productive sector. Attempts were made to maintain a financial structure centred on large, regulated banks, relatively small securities markets and very large parts of the financial system in state hands. In doing so they faced growing competitive pressures from deregulated Anglo-American markets and operators and a growing chorus of propaganda to transfer all those parts of the financial system connected to funding health, pensions and welfare programmes into the private sector under rentier control. The propaganda campaign had a strongly anti-workerist edge to appeal to employers of capital to reduce their tax burdens by favouring the privatisation of these parts of the financial system.

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[46] On this see I.M.Destler and C.Randall Henning: Dollar Politics: Exchange Rate Policymaking in the United States (Institute for International Economics, Washington DC,1989)

[47] Under the DWSR governments except the US, Germany and Japan can have only two of the following 3 features: control over exchange rates, full financial mobility and independent monetary policy. On the general principles, see, for example Charles Wyplosz: Globalized Financial Markets and Financial Crises, paper for Forum on Debt and Development, Amsterdam, 16th-17th March,1998.

But the capitalist classes of Western Europe generally maintained resistance to this campaign, partly for political reasons (fear of future domestic political vulnerability to revolts) and partly because such moves would enormously increase the opportunities for Anglo-American financial operators to acquire sway over their productive sectors as well as their financial sectors.[48] The battles over these issues were fought out mainly between the German and British governments over alternative approaches towards the regulation of investment banks (merchant banks, in traditional British parlance). In late 1992 a compromise EU directive on investment services and capital adequacy standards was adopted, one which favours greater liberalisation in this area.

Thus the spontaneous dynamics of the Euro-land region will lead to the hollowing-out of the nexus of institutional barriers to the triumph of the rentiers because the regional regime is constructed for a competition between regulatory authorities that ensures that the least regulated operators in the financial sector win. Without a strong political authority in Euroland its Euro shield against the dollar will be shielding a financial system and productive sector under the increasing sway of Wall Street and American business.

Japan

Japan found itself in a far more vulnerable position for coping with the new monetary chaos that arose in the 1970s. Because of its dependence upon the US market, it faced one American-induced adjustment crisis after another, has been subjected to great political pressure to establish a managed trade regime with the US and constant attempts by the US to interfere with its internal social relations of production. Attempts to diversify into the West European market met with strong EU opposition, only partially overcome through the British back door. The very dependence of the American state upon Japanese financial flows into New York only fuelled the growth of an aggressive trend in US public opinion towards Japan. By succumbing to US pressures in the late 1980s to loosen Japanese domestic economic policy, the Japanese government found itself unleashing the kind of enormous bubble in its financial system that German governments had always managed to repudiate, and the bursting of bubble at the start of the 1990s plunged the Japanese domestic economy into a long stagnation from which it has not recovered.

Yet in the second half of the 1980s, Japanese elites did start to develop a new accumulation strategy: the development of a strong regional network in East and South East Asia and one not based on West European-style neo-mercantilist regional trade policy, but rather on the export of productive capital into the region to boost regional growth -- the kind of policy so obviously lacking in West European policy towards Eastern and East Central Europe or for that matter in American policy towards Latin America. Through this strategy, Japanese capital could cope with the wild swings of the dollar: a high dollar gave scope for the Japanese domestic base, while a low dollar gave scope for the regional bases of Japanese and Japanese-linked capital to flourish since these economies had exchange rates largely tied to the dollar. The regional economies in turn were exporting to North America and Europe as well as developing intra regional trade and financial flows.

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[48] The huge expansion of the scope for private finance in pensions etc. would require a very large expansion of securities markets, would undermine bank-corporate sector linkages and open Europe’s corporate sector for acquisitions by American finance capital.

This Japanese defensive strategy meshed with the already strong growth in East and South East Asia and greatly re-enforced that growth. The result was to create an entirely new *growth centre* within the world economy and one which has acted like a magnet for capital throughout the rest of the core economies in the 1990s. Thus, the regionalist response of Japanese capitalism to the Dollar-Wall Street system was a stunningly successful one from the point of view of spontaneous economic rationality. Japan was creating a great virtuous circle of dynamic accumulation between its own capitals and East and South East Asia. In purely regional terms this was a far more dynamic solution than that found by German capitalism within the West European arena. But there was also a dimension of great vulnerability. German governments had been able to construct a strong politico-monetary shield in the form of a Monetary Union and a mass political idea (European unity) both of which the capitalist classes of Germany's European neighbours shared. But Japan's regional strategy had no such politico-monetary counterpart. If Germany had, in this field, something like the shield of Achilles, Japan was left with his heel: most of the region in the dollar zone and thus a split in the political-monetary centre of the regional strategy; and no political bloc in the region at either the level of dominant social groups or a popular level. Instead, the region was riven with political suspicions and legacies of earlier hostilities: between China and Japan, between Korea and Japan, between China and Taiwan etc. etc. While Western Europe had overcome hostilities at least as deep, partly with American support in the early post-war years, no such evolution had occurred in Japan's regional hinterland.

The Bifurcation of the South

During the long boom in the post-war period the countries of the South on the whole also experienced high rates of growth: fifty of these countries had average growth rates of over three per cent per year between 1960 and 1975.[49] Total factor productivity growth was particularly high in the Middle East and Latin America: 2.3% and 1.8% respectively -- a better performance than East Asia whose annual productivity growth was only 1.3%.

With the start of the Dollar-Wall Street regime and the oil crisis, a bifurcation began on the basis of one criterion: how well the state concerned coped with the volatile and often savage dynamics of the new Dollar-Wall Street regime. With the oil shocks and the onset of stagnation in the core, the overwhelming majority of countries of the south experienced strain on the current account. They could either borrow massively abroad under the new Dollar-Wall Street regime, or they could make sharp domestic internal macroeconomic adjustments, tightening fiscal policy and devaluing their currencies. Borrowing abroad was the easy option: the Anglo-American banking systems were eager, as we have seen, to lend and borrowing allowed these states to avoid the domestic social conflict that macro-economic adjustment required.

It is important to stress that borrowing from Wall Street was not only easy it was *economically rational* for governments in the circumstances of the 1970s. In 1983, US Deputy Secretary of State Elinor Constable explained to Congress how US government policy created the conditions that would make governments in the South pursuing current economic rationality want to steer a course towards disaster:

"Our policy did not focus on the need to adjust. Rather, our primary concern was the

[49] The data used here are from Rodrick, op.cit.

encouragement of efficient ‘recycling’ of the OPEC surplus -- a euphemism for the assurance that countries would be able to borrow as much as they needed. The incentive to borrow rather than to adjust was strong. Interest rates were low or negative in relation to current and expected inflation; liquidity was abundant; and both borrowers and lenders expected that continued inflation would lead to ever-increasing export revenues and reduce the real burden of foreign debt.”[50] The critical failure on the part of the borrowing governments was to fashion economic policy within a framework of current economic rationality rather than grasping that the entire macro-economic framework they faced could be transformed by *political decisions about the dollar price and interest rates of the US government transmitted through the world economy by the DWSR.*

[50] Statement by Elinor Constable in US House of representatives, International Bank Lending (Washington DC, GPO,1983) page 58, quoted in Kapstein, op.cit.

Those countries which took the borrowing course -- in the Middle East, Latin America and parts of the Soviet Bloc (especially Poland and Hungary, as well as Yugoslavia) -- were then trapped in debt crises and long stagnations of 15 years or more as they were dragged through the ‘structural adjustment’ ringer of the IMF/WB. Those countries which undertook internal adjustment and avoided the debt trap were mainly in East Asia and were able to weather the onset of the new regime and continued to grow.[51] Others were dragged down by the DWSR into a systemically induced series of financial blow-outs. While during the 1970s, the number of financial crises never rose above 5 countries per year. Between 1980 and 1995 the number fell below 5 per year only in two years (1988 and 1989) and in some years the numbers ran at over 10 countries per year. According to the IMF, two thirds of all its members have experienced severe financial crises since 1980, some more than once.[52]

It is important to underline one point about this experience. The ideologists of the DWSR claim that the debt crisis of the Latin American countries (and states in Eastern Europe) was *caused by* the bankruptcy of their earlier import-substituting development strategies involving large state sectors and protectionism. Thus, they had to embrace a new strategic paradigm -- the so-called ‘free market’ one. Yet as Dani Rodrick has shown, the debt crisis and the attendant domestic financial crises in these countries had been caused *not* by their import-substituting, statist accumulation strategies -- in mainstream terms these are *micro-economic* development devices -- but by their government’s failures of *macro-economic* policy adjustment to the impact of the oil price rises and the new monetary-financial system of the 1970s. As Rodrick explains Import Substituting Industrialisation (ISI) “brought unprecedented economic growth to scores of countries in Latin America , the Middle East and North Africa, and even to some in Sub-Saharan Africa” for two decades. “Second, when the economies of these same countries began to fall apart in the second half of the 1970s, the reasons had very little to do with ISI policies per se or the extent of government interventions. Countries that weathered the storm were those in which governments understood the appropriate <u>macro</u>economic adjustments (in the areas of fiscal, monetary and exchange-rate policy) rapidly and decisively.”[53]

Thus, the real pattern of causality in the transformations following the adoption of the Dollar-Wall-Street regime was as follows: a successful development *strategy* faced sudden, large challenges to macro-economic *tactics* produced by the orchestrated chaos of the new international monetary-financial regime. The macro-economic tactical failure led to terrible currency and financial crises and these enabled Washington to impose a new strategic model on these countries. This model was then claimed to be a superior strategy to an earlier failed strategy. Yet the new model was nothing more than a combination of ad hoc solutions to pay off US banks plus a new vulnerability to the dynamics of US capitalism.

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[51] A crucial factors in the capacity to make swift domestic adjustments are the domestic class balance of forces. It may be that the East Asian states had far greater capacity to impose the costs of adjustment on the working class than countries that failed to adjust,

[52] See Charles Wyplosz, op.cit.

[53] Dani Rodrick:”Globalization, Social Conflict and Economic Growth”, revised version of the Prebisch Lecture delivered at UNCTAD, Geneva, 24th October, 1997.

That this was indeed the case became starkly clear when the show-case of the new model, after a decade of stagnation and a short phase of growth suddenly plunged into another terrible financial crisis: the Mexican crisis of 1994-95. Because as a result of the usual ideological mechanisms, the high priests of the Washington Consensus really believed their new model was superior to the ISI model, as 'proved' by the earlier debt crisis, they genuinely could not notice Mexico's extreme vulnerability and fragility and the blow-out was a great shock. But its warning that the so-called Economic Reform free market model was a path only to increased vulnerability in the future was simply brushed aside. It *had to be a good model* because it was the *only model that fitted with the facts of a DWSR to which the biggest economy in the world, American capitalism, was increasingly hooked.*[54]

These crises, then, bifurcated the South into two zones: the new dependencies of the DWSR and the new growth centre in East and South East Asia. The new dependencies themselves contained strong internal differentiations, between political economies which entered a path towards social disintegration (much of Africa) and others which entered a path of stagnation, punctuated by fitful growth (most of Latin America and the Middle East).

The story of the new, post-1980s dependencies has been one of chronic financial instability and stagnation, punctuated by fitful growth and further financial blow-outs. Since 1980, serious financial crises have been happening in one country after another, seriatim and affecting two thirds of the members of the IMF at least once. Each time, the media of the DWSR try to entertain us with juicy stories, full of local colour and detail of local incompetence, corruption or whatever that just happened to cause each individual one of over half the countries of the world turning out to be a basket case. But after a while these stories begin to pall as we realise both that the all the countries of the world seem full of corruption and incompetence causing blow-outs yet while at the very same time the same media assure us that the world as a whole is doing tremendously well, except for one country at a time!

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[54] The Mexican crisis was also interesting as the first big blow-out between the US and Western Europe within the IMF. Mexico was a vital US political interest so it was determined to stabilise it even if that meant using over $20 of West European money to do so. The West Europeans said there was no global threat from Mexico to the international financial system so the US should pay and the BIS would grant only bridging money while the US hunted for funds elsewhere. But Treasury Secretary Bensten persuaded Camdessus of the IMF to announce publicly that the West Europeans *were* fully committing the money, not providing only bridging money. This meant that if the Europeans publicly set the record straight, they could have tipped Mexico over the cliff could have been blamed for a total collapse. For the first time in IMF history, the minutes of an IMF board meeting were made public because European officials leaked them to demonstrated that they had not voted for the bailout (but had abstained).

As a percentage of GDP these financial crises can be extremely costly, especially where they take the form of crises at the heart of the banking system: in the Argentinean crisis 1980-82 these costs amounted to no less than 55.3% of GDP; in Chile, 1981-83, 41.2%; in Uruguay 1981-84, 31.2%; in Israel 1980-83, 30% and in Mexico 1994-5, 13.5%.[55] The IMF has played a central role in distributing those costs, doing so in the active service of the United States but with the passive acceptance of the other G3 states.

East Central and Eastern Europe

The record of these countries under the DWSR since 1990 is overwhelmingly the same story of tragedy as that of most of Latin America in the 1980s. The propagandists of the DWSR have every reason to congratulate themselves on introducing capitalism into a number of these countries, given just how terrible the experience has been for the bulk of the population of the region. Ten years after the process started only one country, Poland has clawed itself back to its statistical GDP per capita of 1989. And the deep gloom across the horizon of the entire region has been lifted only by flashes of lightning from financial crises, exploding in one country after another.

The New Growth Centre

The new growth centre in East and South East Asia included China, South Korea, Taiwan and increasingly also the countries further south. They were unified not by the fact that they all shared the same internal development model but by the fact that their macro-economic tactics enabled them to survive the new international regime of the 1970s, by the fact that they had access to the American market and, in the late 1980s, by the fact that many of them could enjoy an expanding influx not of hot money from New York but of productive investment from Tokyo. They constituted a new growth centre not in the sense that they had strong growth rates but in a much more fundamental sense: they were the one large centre of dynamic, sustained capital accumulation in the entire world.

At the start of the 1980s, the region (excluding Japan, Australia and New Zealand) accounted for only one-sixth of world output. But by the mid-1990s it accounted for about one quarter of world GDP on purchasing power parity-adjusted terms. If this trend had continued, the region would have accounted for one-third of world output by the year 2005. By adding Japan to the aggregate we can see that the centre of the entire world economy was, for the first time in about 500 years shifting out of the control of the Atlantic region.

Similarly, over the last decade the developing countries of Asia have seen their share of world exports nearly double, to about one-fifth of the total. These countries are also taking a growing share of industrial country exports, a factor that helped cushion the impact of successive recessions in the Atlantic area during 1990-93. During the 1990s to 1997, the region accounted for some two thirds of new global investment and for about half of the total growth of world GDP growth. Thus it was becoming increasingly important as a direct stimulator of the economies of the Atlantic world.

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[55] Martin Wolf: ‘The Ins and Outs of Capital Flows’ Financial Times, 16th June,1998.

And it was achieving these results without clashing with the international logics of the Dollar-Wall Street regime and the Anglo-American rentier interests entrenched within that regime. Thus Michel Camdessus liked to stress the wonderful opportunities offered by some of the stock markets of the region to Western rentier capital: for example, in Hong Kong, Malaysia, and Singapore, stock market capitalization as a share of GDP, exceeds that of France, Germany, and Italy.[56] He also, of course, would make the spurious claim that the inflows of speculative Atlantic funds into these securities markets in the 1990s were a kind of net aid for the development of productive capital in the region. The reality was exactly the reverse:

In his Per Jacobsson Lecture to the assembled central bankers and government officials in Hong Kong for the IMF/World Bank meetings in September 1997, the Chief Executive of the Hong Kong Monetary Authority explained the situation as follows:
"Much of Asian savings, in particular official sector savings and private sector savings that have been institutionalised, are still invested in assets of OECD countries.....insofar as Hong Kong is concerned, in excess of 95% of our US$85billion of foreign reserves are invested outside Asia. Specifically, in the management of our foreign reserves, we work against a preferred neutral position of about 75% in US dollar assets, mostly in US Treasury securities. I understand also that more than 80% of total Asian foreign exchange reserves amounting to US$600billion are invested largely in North America and Europe....It can be argued therefore that Asia is financing much of the budget deficits of developed economies, particularly the United States, but has to try hard to attract money back into the region through foreign investments. And the volatility of foreign portfolio investments has been a major cause of disruptions to the monetary and financial systems of the Asian economies. Some have even gone so far as to say that the Asian economies are providing the funding to hedge funds in non-Asian countries to play havoc with their currencies and financial markets. This comment is perhaps a little unkind.....But *there certainly is a problem with the effectiveness of financial intermediation in this region, which is inhibiting the flow of long term savings into long term investment."*[57]

The American Political Economy

The construction of the DWSR has had important feedback effects on the US financial system and economy, while endogenous US developments have exerted important and growing effects upon trends within the DWSR.

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[56] Globalization and Asia: The Challenges for Regional Cooperation and the Implications for Hong Kong Address by Michel Camdessus Managing Director of the International Monetary Fund at a conference sponsored by the Hong Kong Monetary Authority and the IMF on 'Financial Integration in Asia and the Role of Hong Kong' Hong Kong, March 7, 1997

[57] Per Jacobsson Lecture on Asian Monetary Co-operation by Joseph Yam, JP, Chief Executive of the Hong Kong Monetary Authority, Hong Kong, 21st September 1997

The American financial system has had one structural feature which has made it very different from almost every other capitalist system: the extraordinary fragmentation of its banking system. Whereas almost every other capitalist system tends to have large, national retail banks dominating the credit system and having a close inter-relationship with the state at a central level, this has not been the pattern in the United States.[58] In the changing economic conditions of the last quarter of a century, new forces have emerged in the American financial system, filling what one might describe as the void left by the fragmentation of the banks. And as these new forces have arisen, they have escaped from the kinds of regulation needed to prevent the most dangerous kinds of vulnerability from becoming entrenched.[59] We can list a number of the most significant changes.

First, there has been a dramatic decline in the role of the commercial banks in the supply of credit to the productive sector, with the rise of the so-called mutual funds. These organisations offered credit to companies in the form of bonds instead of bank loans. The company would issue bonds bought by the mutual funds. The mutual funds then can offer savers a higher rate of interest on their deposits than the banks could offer. The depositors would benefit also through the diversification of the mutual funds' holdings of bonds and other securities (paper claims for royalties that can be bought and sold in financial market places). Thus the supply of money capital to American employers came to be tied in to the rise and fall of prices on the securities markets. And the savings of Americans of all classes came also to be tied in to price movements on these markets. The scale of the funds in these Mutual Funds has soared until it is as large, if not larger than the deposits within the entire American banking system.

The second major trend has been the breaking down of the walls between different sectors of finance. The rise of the mutual funds was followed by banks being able to develop their own mutual fund operations and thus become more and more involved in stock market trading. The American Savings and Loans institutions (the equivalent of Building Societies) were deregulated so that they could trade in securities and start acting like commercial banks. And in these ways the entire American financial system has been sucked into the vortex of the securities markets, a formula for opening the financial system to strong speculative pressures.

The third major change has been the development of a very large range of new types of securities. Mortgage contracts, for example, have become tradable bits of paper. So-called junk bonds with very high interest rates, used to amass huge quantities of funds for buying out companies, became very popular. And a whole new tier of securities, called derivatives,

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[58] This central role for very large national banks is true not only in Japan, France and Germany (which has also had strong Land banks) but also in the UK and in the former British dominions like Canada. Italy alone among the G7 countries approaches the US in its lack of strong national banking pillars in its financial structure.

[59] It is, of course, true that some parts of the US financial system remain subject to what UK operators would regard as ferocious and tight control: the powers of the Securities and Exchange Commission are immense. But they regulate the activities of those involved in the stock exchange only from the angle of personal probity and not for the purpose of minimising macro-economic risk.

has grown enormously. They involve trading in securities whose prices are derived from the movements in prices in other, primary securities or currencies. The great bulk of derivatives trading is unregulated because it takes place ‘over the counter’ (OTC) between two institutions, rather than through regulated exchanges. One important effect of the growth of derivatives trading is that it links together price movements in one market -- say, shares or bonds -- with price movements in another -- say foreign exchange. Shocks in one market thereby become much more contagious to other markets than in the past.

The fourth major change has been the rise of the Hedge Funds. The name is a euphemism: these are speculator organisations for making money through the buying and selling of securities on their own account to exploit price movements over time and price differences between markets. The biggest of these hedge funds are not marginal speculators. They are the offspring of the very biggest of the investment banks and the mutual funds. Hedge funds are not necessarily called by that name. Thus Goldman Sachs, which is a partnership, is largely a hedge fund: in other words the bulk of its profits in 1996 and 1997 derived from speculative trading on its own account. Salomon Brothers was also, in essence a hedge fund. Since the banks are not allowed to engage in speculative activity, their managers have helped to establish hedge funds that *are* allowed to do so, because they are not banks but partnerships, often registered off shore for tax-dodging purposes. The biggest of the banks then lend huge sums of money to what are, in effect, their creations, in order that the hedge funds can play the markets with truly enormous resources. This scale of resources is vitally important because it enables the speculator to shift prices in the market in the direction he wants the prices to move in through the sheer scale of the funds involved.

We will return to this issue of market power later. But it is important to stress the capacity of the hedge funds to use huge loans from the banks and from mutual funds to play the markets. These borrowings are known, in the jargon, as ‘leverage’. According to IMF studies, hedge funds can be using, at any one time loans twenty times their own capital. Soros, boss of one of the biggest funds, has said he was able to gain leverage 50 times his capital for his operations. But it now turns out that Long Term Capital Management was able to be leveraged 250 times its own capital. With a capital base of $2.5bn it could, in other words, wield about $600bn of funds. If we bear in mind that the total capital of US hedge funds in 1997 was estimated to be about $300bn and assume that average leverage is 50 times the capital base, we get a total financial power of a staggering $15,000Bn -- a speculative strike force of this dimension or larger has thus been built up at the very heart of the American system. And it is a force which is completely unregulated.

The final structural change in the US financial system during the last quarter of a century has been an enormous growth in its exchanges with the rest of the world. All the key players in the domestic market -- the mutual funds, investment and commercial banks and the hedge funds have become more or less heavily involved in international business. The most dynamic sector of growth has been the foreign exchange market and the foreign exchange derivatives markets, which are overwhelmingly unregulated OTC markets. At the same time there have been huge growths in the flows of funds into and out of the American financial markets from around the world and the big American institutions have spread their offices across the globe as other financial markets have been pushed open.

Two general conclusions can be drawn from this brief summary: first the securities markets in the United States have become very large in terms of the volumes of business which takes place in them in normal times. This gives them a quality which is highly prized by the holders of interest-bearing capital: the markets are, in normal times, highly liquid -- in other words, anyone wanting to sell and leave the market can normally do so very easily, just as anyone wanting to buy can easily find a seller. But the second conclusion is that the inner structure of the whole financial system has become strategically very vulnerable to crisis. All the accumulated experience of credit systems under capitalism points to the fact that the American financial markets are far more vulnerable to a hideous collapse as a result of the disintegration of the regulatory order, the increasing centrality of the securities markets, the huge growth of extremely risky new types of securities and the extraordinary rise to dominance within the whole system of speculative funds. Even in the banking sector where stronger regulatory supervision is supposed to prevail, this control seems to have largely broken down. One recent survey found that only 3 out of 100 US banks were observing the regulatory rules fully.

The question therefore arises as to why the American state has allowed this set of developments to occur and continue unchecked. The most straight forward answer as to why this extraordinary strategic vulnerability has been allowed to spread through the US financial system is that the regulators themselves are closely linked to the big speculators. The US Treasury Secretary Robert Rubin is himself a speculator by profession, since he comes from the management of Goldman Sachs. Greenspan at the Federal Reserve has spent his whole life playing the markets when not in government. Federal Reserve Board members move continually through revolving doors between Washington and trading on the markets. This explanation no doubt contains an important truth, yet so much is at stake that one might expect the other areas of will formation within the American state to step in and assert control: the Presidency and Congress, for example.

A second explanation might be that these other instances of government have themselves become dependent upon the financial operators for campaign funds: they have in large measure become the cronies of Wall Street. This is factually true. As Rothkopf has demonstrated, Democratic Party Chairman Ron Brown pointed out to Clinton the importance of developing economic policies that would appeal to Wall Street in order to tap into huge pools of potential campaign funds there.[60] This again, no doubt has force, but there are other immensely powerful centres of American capitalism outside the financial markets, which would surely cavil if the decisive control of the political establishment had been *captured by* speculative finance.

Yet another explanation might be that all the strategic social groups within American society have themselves been captured by the institutional dynamics of the financial markets. The income and wealth of the managements of the big corporations have become tied to future prices on the stock and bond markets, have invested their savings in the investment banks, mutual and hedge funds and have been restructuring their own corporations to make the augmentation of ‘share-holder value’ their governing goal. And American workers also have come to rely upon the securities markets for their pensions, health care and even their wages, which have been increasingly combining cash with securities. Any regulatory drive would

[60] Rothkopf: Mad Mercantilism (Council on Foreign Relations paper, 1998)

inevitably have a depressive effect on current activities and would therefore cut the politicians involved in pushing for the regulation off from important and broadly based political constituencies.

This political barrier is then powerfully buttressed by the rentier ideology of laissez faire and free markets. But the power of ideology should not be exaggerated. The lives of workers in modern capitalism are tied to capital not only through the wage relation, but also through the savings relation. If the savings relation is mediated through the state, as in Western Europe, workers' security is less tied to market developments and rentier interests. But if the savings relation is in the direct control of private financial markets, then workers themselves acquire a rentier interest.

Such does, indeed, seem to be the political situation within the United States in the 1990s. It is in large part the result of the attempts by successive administrations to exploit the DWSR in supposed American capitalist interests. Whether it has strengthened the foundations of US capitalism relative to others we shall explore below. But it has had spreading narcotic and addictive effects through the US domestic political economy and has greatly encouraged the drift towards financial vulnerability.

And with the arrival of the Clinton administration the evolved DWSR has become more than an instrument for gaining quantitative molecular gains from US financial and monetary dominance. It has become radicalised as the activist programme for establishing a world imperium and it has also found its place at the very heart of the Clinton administration's political strategy for world order.

The DWSR and the Dynamics of Domestic Socio-Economic and Ideological Change

This account of the impact of the DWSR on political economies has at every stage pointed towards the way the regime, through the mediation of political economies, transforms socio-economic structures within the states of the world. It does so by generating social conflicts within states, conflicts which the DWSR regime ensures do not take place on a level playing field: certain social groups within a state can exploit the DWSR in crisis situations in order to strengthen their domestic political and social positions.

We can present the pattern very schematically: when a financial crisis occurs, certain social groups can gain from IMF/WB restructuring proposals. Money capital can escape to Wall Street and the restructuring package will tend to strengthen its domestic social position; privatisations of state industries to restore state finances again benefit those sectors of the capital class with access to large funds of money. Export sectors can benefit from the restructuring package as well, and capital as a whole finds in the IMF package a way of imposing its rule over other, subordinate social groups. The sectors of domestic capital that are weakened are those engaged in import-substitution, while those supplying staple products for domestic markets will tend to be taken over by foreign multinationals provided with new access to domestic assets by the IMF package.

None of these outcomes is *automatic*: they depend upon domestic political struggles between social groups, political struggles whose outcome depends upon the political structure of a state and the balance of political forces within it at the time of the crisis. And despite the IMF/WB efforts to impose a one-size-fits-all standardised package, the exact algebraic forms (not to speak of the arithmetic ones) of these outcomes will vary from one state to another. To take an obvious example, there have been great variations in the algebra of privatisations in the former Soviet Bloc. And the impact of the outcome within the society is typically a new round of social and political conflict involving a backlash against the outcome. That is why the social and institutional engineers of the IMF/WB make great efforts to ensure that the package is robust against expected backlashes.[61]

Nevertheless, the general trend has been one of at least partial success in social transformation for the alliances of domestic social groups and the IMF/WB. This does not of course mean sustained macro-economic success -- far from it: new crises are typically just around the next bend in the road. But whatever the government thrown up by the backlash, it will face a new social balance of forces in its society and one which it will largely have to accept if it wishes to avoid new financial turmoil -- panicking the markets. Thus a deepening social transformation of the internal social dynamics of states is produced by the DWSR.

These changes then feed back onto transnational ideological life. The deepening transnational social gleichschaltung generates an increasing international convergence in the field of ideology, whose highest expression is the 'Washington Consensus'. The origins of the consensus at first sight appear to be a mystery. It is presented as the result of a purely intellectual learning curve: how people have learnt that so-called statist strategies do not work or do not work as well as 'free market' rentier strategies. Yet this explanation for the consensus cannot be true, since the old statist strategies seemed to work better in the past than the new free market strategies have worked in the contemporary period (the last quarter of a century). And the only really dynamic economies in the recent period have been those of East and South East Asia some of which have had highly statist strategic mechanisms.

The truth, of course, lies in turning the relation between the ideal and the material upside down: it was not the Washington Consensus idea that taught people to transform social relations; it was the material transformations of social relations which produced the power of the Washington consensus idea. And the whole process was driven not by a quasi-legal regime of rules and norms and principles in an issue area, but by the mighty material forces of money and finance in the DWSR. As soon as this transnational socio-economic regime started to crack so too would its reflection in the Washington consensus.

PART FOUR: DWSR, POWER POLITICS AND THE CLINTON ADMINISTRATION

So far we have attempted to explain the mechanisms of the Dollar-Wall Street Regime, to show that it reproduces itself as a political as well as an economic mechanism, steered by the joint actions of US governments through their dollar policies and control of the IMF/WB and of the US-centred international financial markets. We have also tried to trace, in rough outline some of its effects upon national political economies and the social structures of

[61] For a detailed and fairly comprehensive survey of the tactics used for attempting to make the social engineering robust against backlash, see J.Williamson (ed.): The Political Economy of Economic Reform.(Institute for International Economics, Washington DC, 1996)

states. We also sought to minimally demonstrate, from the way both US dollar policy and the US attitude to international financial regulation and to the roles of the IMF/WB have operated, that the DWSR was run from the angle of US national interests. But the question we must ask is: how are we to understand national interests under contemporary capitalism? How can we arrive at a general conceptualisation of the political and economic interests of a leading capitalist state? This is the issue which we want to address now in order to try to provide a framework for understanding the radical activism of the Clinton administration in its efforts in the international political economy.

A. National Interests and International Challenges

Mainstream Theories of State International Economic Interests

Mainstream economics and political economy tells us that the economic interests of capitalist states should produce no international political conflict whatever about economics as such, except for transitional adjustment frictions, provided a state's political leaders act in their own rational self-interest. These interests are defined as the following: first, growing long term prosperity for their domestic population through raising domestic productivity -- high productivity in one state does not weaken the drive for higher productivity in others; second, exploiting the advantages to be derived from the international division of labour by adhering to free trade; and thirdly, maintaining co-operation with other governments in an effort to manage effectively international macro-economic flows. With growing prosperity, the state's own revenues will rise, giving it great international political power. So, according to this view, the international interests of states are essentially harmonious with those of other states, provided the others retain similar, open rational policies.[62] Thus, the mainstream theory suggests that the attempts by states to engage in political intervention in international economics are the result of certain special interests within the state trying to use their political influence on the government for 'rent-seeking' advantages which are actually damaging for the wider economic interest.

Mainstream economics does acknowledge that adjustment tensions can arise between states as a result of international payments imbalances. These can result in states being tempted to impose protectionist restrictions on imports on subsidies for exports in order to escape the need for domestic adjustments. A robust international set of rules is needed to prevent such ultimately self-defeating attempts by states to escape the need for internal adjustment.

Mainstream theory then adds extra sophistications connected to the supposed rise of economic interdependence, whereby the domestic actions of governments can have unintended transnational spillover effects within other domestic political economies and these then require the development of new international regimes for co-ordinating national policies in more and more fields. But such extra dimensions are presented essentially as technical responses to technical problems within a basic framework of deep harmony between the national economic interests of powers.

This mainstream economic theory dove-tails well with mainstream pluralist political science. This views politics in a liberal democracy as a competition between parties for the votes of

[62] A useful restatement of these positions is found in Krugman: "Competitiveness: A Dangerous Obsession" Foreign Affairs, March/April,1994

citizens whose preferences are guided by a self-regarding concern to maximise their own welfare. Since such welfare is concerned with increased individual prosperity, voters push governments to direct all their efforts towards economic growth and national prosperity. And governments will thus gain their optimum political pay-off by pursuing these goals in the ways prescribed by liberal economics which holds the key to assuring their populations' prosperity and thus producing satisfied voters. Again, there are dangers that particular groups of voters will try to capture the political process in search of 'rent-seeking' advantages which will enhance the private welfare of sectional interests at the expense of overall welfare maximisation, but these special interests can be and should be suppressed through the appropriate design of systems of democratic accountability.

These mainstream economic and political science views sit slightly uneasily with the mainstream International Relations theory of 'Neo-Realism': this argues that states are driven by the inescapable characteristics of the inter-state system into a struggle for relative power -- power relative to other states. Because states exist as isolated entities in an anarchic world where security can be guaranteed only by each state maximising its own power relative to other states, there is a ceaseless struggle between states for power.[63]

Reconciliation between these mainstream disciplines is achieved through the Neo-Realists' claim that in this ceaseless power struggle, states are interested overwhelmingly in the coinage of military capacity: economics is of little interest to them.

But in recent years, neo-mercantilist theories have enjoyed a revival against mainstream liberal political economy. This is less a coherent body of theory than a view that international economic outcomes are profoundly shaped by international political conditions and forces.[64] But from this starting point the neomercantilists argue that the hierarchical international division is labour is 'path dependent' and is not the product of spontaneous free market outcomes. This path dependency is established through states manipulating markets to prevent the 'normal' operations of international markets, as envisaged by liberal international economics. As a result, then, of the impact of the inter-state system on international markets, there is an inevitable political struggle for national prosperity between states as each state tries to use its external political influence to manipulate its external environment for national advantage in trade. These kinds of views can accord with Neo-realism but clash with mainstream neo-classical economics at a cognitive level (even if those holding a neo-mercantilist view of what actually happens share liberal views as to what should happen).

The problem with these different theories is that while they seem to provide explanations of much of what goes on in international relations, they also seem to miss a great deal. Mainstream economics reminds us of the central importance of domestic productivity and of

[63] The classic statement of this position is found in Kenneth Waltz's work.

[64] The work of Robert Gilpin has done much to revive this trend of thought as a means of understanding international economics. His work in this field began at the start of the 1970s with "The Politics of Transnational Economic Relations" International Organization, VolXXV, No.3 1971.

the value of international macro-economic co-ordination. But it leaves an extraordinarily large burden on the idea of welfare-destructive 'rent-seeking' to explain the great swathes of activity in the international political economy which clash with its norms. To take a simple example which is completely irrational from a mainstream economic point of view: the wild dance of the dollar over the last quarter of a century has been completely irrational from a mainstream point of view: can it really be explained by certain groups 'rent-seeking? And if it is to be explained like that, surely some groups seek rents from a high dollar and others from a low dollar. So how do we explain the seeming musical chairs among rent seekers within the span of single presidencies?

As for neo-mercantilism, it offers an explanation of everything that the mainstream fails to explain but by the same token fails to explain everything that the mainstream does explain -- the mixture of co-operation as well as conflict between the great capitalist economies. Neo-mercantilism would suggest that there should be a state of almost permanent economic warfare between the main capitalist states. Yet the degrees of tensions between them vary greatly through time and across space.

To make sense of the national interest in economics, we will suggest that these theories suffer from a common weakness: they lack any mediation between the 'economic' and the 'political', with the economic defined as 'growth', 'prosperity', 'jobs' or productivity. They thus take for granted what needs to be investigated: what kinds of social institutions actually control access to 'growth' etc? What are their compulsions and how do their compulsions and interests operate in domestic politics to structure the definition of the national interest? We need a theory which includes these social mediations between the 'economic' and state political action on economic matters. One obvious such mediation is provided by the concept of *capitalism as a social system* which gives a twist to the behaviour both of the economy and the state.

We will not attempt here to furnish an alternative theory of the national interests of *capitalist* states: this would require a fully fledged theoretical alternative to mainstream social science. We will simply suggest some conceptual rules of thumb that may help to produce a more nuanced appreciation of the extent to which powerful capitalist states may define their national economic interests in ways that allow for both the co-operation sought after by mainstream economics and for the conflict stressed by neo-mercantilism.

A Rough Concept of Capitalist States' National Interests in International Economics

Within a capitalist economy, elected politicians surely do want what mainstream economics says that they should want: ever higher productivity and growth. But such matters are not directly in the government's hands: they are in the hands of private capital which owns the productive labour. Democratically elected politicians, therefore, must serve the special needs of the employers of capital because it is this group which takes the decisions about whether there will be investment and growth. Thus the national interest in economics has to be conceived as the national *capitalist* interest, insofar as the capitalist social group exercises sovereignty over economic life.

Private capitalists do not want growth as such: they want capital growth and security. And these goals do not have to come from actions whose end-result is expanding national production. They can come from one capitalist concern extending its control over existing production in the sector. If they face competition, then one of the ways of tackling that competition is through a drive to raise their productivity, lower their unit costs, improve quality and thus try to sell more units and thereby attract a larger share of the market. But there are other ways of overcoming the competition: using the size of your capital for strategic action to destroy smaller rivals or potential rivals or co-opting your rivals into a cartel to control the market. And with monopolisation in a closed economy, it is by no means obvious that expansive investment for higher output is the royal road to further progress of capital growth. And if the market is already saturated and controlled, it is not obvious that very large new investments in new technologies (the key to rapid and sustained productivity growth) are rational.

The economic pressures towards monopolisation are very strong in advanced capitalist economies because advanced industry tends to have very high capital-output ratios (or, in Marxist terminology, a high organic composition of capital). Each extra £ of capital investment produces only a small extra-amount of value added. Very large investments in fixed capital are needed to enter the sector and capitalists who make such outlays need to be assured of long-term control of markets in order to realise an adequate return on their capital. This kind of capitalist enterprise has certain compulsions: to block new entrants to its markets; and to control prices to assure adequate long-term return on fixed capital investments.

Another very important feature of advanced industry is the fact that it tends to benefit from important economies of scale. Thus, the greater the market share a company can acquire, the more effectively it can compete with potential rivals. Thus companies have a compulsion to expand market share to assure maximal scale economies.

In earlier conditions of many small capitals competing within domestic, pluralistic markets bankruptcies on the part of market leaders have few serious consequences for the state. But if big monopolies collapse and foreign monopolistic enterprises capture the market, this has serious consequences.

The productive sectors of the national economies of the leading capitalist powers are indeed highly monopolistic today. They seek to maintain control over their markets through blocking new entrants and through 'centralisation of capital' -- big companies gobbling up small -- and through concentration of capital -- developing production systems to gain maximum scale economies. States are also enlisted to solve these problems both by providing large state-markets for monopolistic industries and by providing a very large range of support services (infrastructures, labour training, etc) for these monopolistic companies.

In conditions where the main markets for such quasi-monopolistic industries are expanding internationally and where a state's capitals in those sectors face no serious international competition, there are likely to be high rates of investment and technological innovation as the companies concerned feel assured of future capital growth. But where new entrants challenge these quasi-monopolies successfully for market share, very great problems can arise: new large investments in fixed capital become extremely risky, profit margins are cut by the new competition and even the biggest companies can face the risk of bankruptcy -- economic collapse.

If this is a roughly accurate picture then we can explore its implications at an international level. The capitals of the main capitalist states operate internationally for a number of objectives. First for raw materials needed in their production process and not available domestically. Some of these materials are so vital -- energy and strategic goods like aluminium, bauxite, copper etc-- that they cannot leave matters wholly to the market: their state is enlisted to use political influence to assure supply. Another need is to control international markets in conditions often of acute competition. In the face of this, as with securing raw materials, national capitals will ‘rent-seek’: try to enlist their state in their cause, to help beat the competition. But the term ‘rent-seeking’ is hardly an appropriate one since it is *a necessary, systemic requirement in conditions of monopolistic rivalry*. And they have another international need: to gain access to external sources of labour -- either very highly skilled labour sources in high tech fields -- or low tech cheap labour for doing the labour intensive parts of their internal labour process. The state can also help in these areas.

Against this domestic capitalist background we can ask what the rational role for the given advanced capitalist state is. The state is not, of course, simply its elected politicians: they come and go but the state must remain and it is the task of the top civil servants to present their political masters with the facts: the systemic facts of the state’s situation and interests within a much longer time horizon than the electoral cycle. From this angle, the state must attempt to ensure the best possible conditions for its capitalists to want to invest and improve productivity and expand output -- the material basis of the state’s own resource strength. Since it is up to capital whether it does these things or not, the state has an overwhelming interest in serving its most important capitals. And since these operate internationally it must seek to serve their international interests. Insofar as they send streams of revenue and profits back to their home base and insofar as they extend their control over overseas markets, the state will consider its international position stronger: the better placed its capitals are in world markets, the stronger its position and influence.

This might suggest that in generally stagnant conditions in the core countries, there will be a war of each against all. If a state’s main monopolies are threatened by the behaviour of the monopolistic enterprises of other states, there will be acute inter-state rivalries. But there tends to be an international division of capital as well as an international division of labour. Not every advanced capitalist state has a big international car company. Only some do. The British state was prepared to give up the struggle to maintain its car companies: it had other international champions (it hoped), such as its financial sector, military industries, pharmaceuticals etc. Matters would be very different for Germany if its car companies were being shut out of international markets. But Germany in the post-war period has not made a central priority to build a large, internationally dominant set of financial markets. Both states will seek to ensure that the interests of their key sectors of capital are well protected internationally. Across most sectors there may be a ‘capital fit’ between two states. Then they can co-operate, perhaps each helping the other in a joint negotiating effort with third states.

The extent to which advanced capitalist states can co-operate in these ways is shown by the recent history of the EU, and most especially by the history of the Single Market. While presented as an attempt to break down barriers to international competition within the EU, the Single Market enabled each member state to encourage its national champions to extend their national monopolistic power and then to find ways to co-operate with others in their sector within the EU so that they could work together in a monopolistic 'division of capitals'. Such efforts at co-operative cartelisation work more easily in some sectors than in others, the Single Market has not been fully implemented by any means and cartelisation tends to be unstable. Nevertheless, the programme has been far more successful in maintaining and deepening inter-state co-operation than any neo-mercantilist theorist would have predicted.

At the same time, the success of the EU states in achieving regional co-operation would have been impossible to achieve had it not been for the great value of the EU for its member states as a lever for international influence over the rest of the world economy. The EU acts as a powerful co-operative operation of European capitals for pressing together for a number of international objectives

1. Each member state can use the EU's trade regime to block competition from imports into the EU from outside.
2. The member state can use the EU as a very powerful lever in international diplomacy concerning the organisation of the international political economy:using the threat of exclusion from the EU market against those external states reluctant to open their markets.
3. The EU trade regime does not cover export promotion on the part of member states, so each can take what measures it wishes to promote the interests of its monopolistic national champions abroad.

In conditions of stagnation within the core economies, the search for new openings outside the core is a central pre-occupation and the EU provides a very valuable collective service for its member states in these tasks.

The National Interests of the Dominant Capitalist State

Against this background we can consider the interests of the dominant capitalist state within the international system, the United States. It gains enormous advantages from being the dominant military-political as well as from being able to dominate the mechanisms of international economic management. This gives it far greater capacities to change its international environment to its advantage than any other state. The DWSR is a central example of the premiums of dominance. The whole world is its sphere of influence and it wishes to assure its continued dominance through the continued strength of its capitals internationally. And it has a far wider range of sectors than other capitalist powers in which it seeks to ensure the dominance of its capitals.

For the leaders of the United States, a capitalist map of the world looks very different from a natural geography map. Quantities of territory as such have little significance except in terms of geostrategy and the resulting basing and logistic requirements. What counts are, in the first place, localities with economically strategic raw materials (oil etc.). These must be firmly under control if possible: a sine qua non for maintaining dominance. But otherwise what stands out are quite small territorial areas: those with today's and tomorrow's key pools of labour and key markets particularly for the decisive sectors of US's capitals. Command over very highly skilled labour in the sectors of the future and over the machines that it produces is really vital. But the value produced by this labour can only be realised through international market sales. In the 19th century, the markets for the sales of goods produced, say, by British labour, tended to be scattered all over the world in the small wealthier classes of every country. In the contemporary world, on the other hand, the really big markets tend to be much more concentrated in small areas where the bulk of the skilled labour also lives: North America, Wester Europe and Japan. It follows that for the leading capitalist state seeking to strengthen its capitals, dominance in these rather restricted areas is crucial. But the lead state must also view this issue dynamically and look at where the key skilled labour pools and markets of the next quarter of a century are likely to appear and gain control of the bulk of the streams of value from these. As for the great mass of the earth's territory outside these areas, it is of little significance and the people who live there can be of no more than auxiliary interest, of even of no interest at all, except insofar as one has to contain disturbances and a slide into forms of barbarism that may have international spillovers.

Within this framework, beyond the general principle of assuring the continued dominance of US capitalism, we cannot say the extent to which there will be conflict or co-operation between the US and other parts of the world. Answering that question will depend upon how much of a fit there is between the need for the American state to ensure that its capitals in key sectors dominate the key geoeconomic areas and what is going on in these areas. But we can say one thing: any attempt by any power to exclude the US from having assured entry for its capitals into these central pools of labour and markets, let alone an attempt to throw a ring around that area to develop it as a regional launch pad for an assault on US capitals in key sectors would produce a savage American response.

Thus, the US interest is to ensure beyond serious doubt that the other main capitalist regions are securely, institutionally open to its capitals and that there is no risk of these regions suddenly becoming closed to US capitals, perhaps as a transitional step to that region acquiring greater strength in the international division of labour than the US has.

The US, in such circumstances, need not constantly fear that other parts of the world may be growing faster than the US domestic economy, as mercantilists would claim: after all, this growth should be a growth for the US companies playing a decisive role in these areas. On the other hand, any region which excluded the US while it was growing dynamically would be an adversarial region.

One final point in relation to US strategy should, however, be mentioned. Insofar as the US retained dominance in the financial field, the US and its capital would want to be able to exercise that financial power in order to be able to take over capitalist companies in other regions, where possible. Financial strike power offers this opportunity for taking over competitors for market dominance, but it does so only if the legal rules in the other regions are such that hostile take-overs of companies are legally possible. Thus openness should mean more than just the ability of US companies to establish their own undertakings in other political economies. It should also mean that the relations of production, including the legal forms of corporate governance and the rules for take-overs, should be friendly towards such efforts on the part of US operators in key sectors for American capitalism to move in and take control of domestic markets.

Against this background, we can see that, contrary to the advice of current realist theorists of international relations, the US will want to cut its military cloth to fit its drives as a *capitalist* state: military power is not an end in itself. But we can also see that the great advantages which the United States could derive from the Dollar-Wall Street Regime through its dominance within it are by no means a sufficient condition for assuring US dominance.

Dominance over international monetary and financial relations is not everything. It needs an anchor in dominance within the productive sector of the world economy and indeed without dominance in that sphere, control over international money and finance remains ultimately fragile.

We can thus try to use our rough theory as the basis for a set of hypotheses:
1. That the US government, acting rationally, should wish to ensure that its capitals in its key sectors would gain control in the most dynamic regions of market growth.
2. That it would want to ensure that the most dynamic pools of labour and of product markets should be maximally opened to its capitals.
3. It would react with extraordinary and emergency measures to prevent the risk of exclusion from such markets.
4. That it would require institutions to be built that could ensure structured dominance over the key geographical areas which were the main centres of international surplus-value extraction.
5. It would gear its steering of the DWSR towards achieving these ends, unless it had other more appropriate instruments of statecraft for doing so.

The Pattern of International Capitalist Dynamics in the Early 1990s.
In 1993 when Clinton came into office, after twenty years of the DWSR, the US's overall share of world GDP was roughly in the same position as it had been in 1970. But there were a worrying new symptom of weakness, not present in 1970. This symptom lay in the US balance of payments. There had been a deficit in the late 1960s and early 1970s. But the deficit at that time could be explained by non-structural factors: the Vietnam war and the very large flow into Western Europe of US productive capital to take up large positions within the EEC market, positions would generate a future stream of earnings into the US current account. But by 1993 there was a serious structural deficit in the current account. And it derived both from a trade deficit and from the need to service an ever growing US international debt position. The American state had allowed its debt to grow to 70% of GDP. The current account balance is not a trivial indicator. It demonstrates whether a state's capitals are earning more from the rest of the world than vice versa.[65] The trade deficit pointed to increasing US competitive weakness in its productive sector. If the current account is not in surplus, then the position of the state's currency can never be completely secure. Of course, seigniorage from dollar dominance gives the US far greater freedom from this payments constraint that any other state. But it is still a sign of weakness, that could count in a crisis. And servicing those weaknesses in the current account had, by the 1990s, come to depend upon the co-operation of an 'ally', (though one increasingly branded in Washington as an 'adversary'[66]) Japan. The Japanese government was helping the US

[65] Because of current account combines both trade in goods and invisibles, including the stream of earnings from MNC production abroad and debt servicing, it is the most useful indicator of a state's basic economic relationship with the rest of the world.

[66] In the draft US Senate trade bill, in 1986, one of its sections began: "When trading with adversaries, like Japan....."Such language has become standard in Washington. See C.Michael Aho:'America and the Pacific Century: Trade Conflict or Co-operation?" International Affairs,69,1, (1993).

Treasury with a continual flow of Japanese funds into US Treasury bonds.[67] One of Bush's final acts as President had been yet again to try to bully the Japanese government into weakening itself to suit the US, this time over competition in the car industry. The result was humiliating for Bush and disquieting for US elites. The Japanese had simply brushed Bush aside and had shown self-awareness of their role in bankrolling the US government.

We must therefore look at what lay behind this current account weakness and summarise the general situation of US capitalism within the wider dynamics of international capitalism. A whole American literature has grown up around the thesis of what is called 'declinism' -- the idea that the US is following in the foot-steps of pre-1914 Britain down a primrose path to everlasting weakness. While this literature was much exaggerated, the comparison with Britain in the early part of the century is nevertheless instructive.

Indeed, the contemporary pattern of political-economic interactions bore significant parallels (As well, of course, as differences) with the dynamics of the international system at the turn of the century: the key units for analysis in both cases are the following: the lead country, the core competitors, the new growth centres, the dependent support-regions, and organised labour.

[67] The inflow of funds didn't come only from Japan: the biggest inflow actually came from the UK and very large flows also came from Holland. But the Japanese bought a lot of the Treasury debt..With the fall of the dollar in the late 1980s, these Japanese mainly private holders of US saw over $200bn wiped off the value of their holdings as a result of this dollar devaluation. Thus, in the 1990s, the US government came to rely increasingly upon Japanese state funds flowing into Treasury bonds. Thus, the stability of the system came to depend upon the political commitment of the Japanese government to US stability. On this, see Susan Strange: Mad Money (Manchester University Press, 1998)

The respective lead countries were of course the UK and the US. In both cases, the lead countries 's economies had grown for a whole historical period through inter-action with the rest of the core: for the UK that had meant Western Europe during the 19th century; for the US it had meant Western Europe and Japan during the post-war boom. In both cases the end result was a strong competitive challenge from the rest of the core as it caught up and started eating into the market of the lead country. Stagnationist tendencies appeared within the core in the late 19th century and in the 1970s. Tensions also arose within the core, exacerbated by political shifts such as the unification of the German states into a single entity in 1871 and the development of bloc tendencies, notably in Western Europe from the 1970s.[68]

In such circumstances, there were powerful pressures from within the core, and notably from within its lead country, to look outwards beyond the core to exploit opportunities in the hinterland for solving internal problems in the metropolis.. One part of the hinterland may be called dependent support-regions. For Britain, this was, of course, the Empire, above all the Indian empire. Products losing competitiveness within the core could be dumped in Empire markets, whose internal social relations of production could be restructured to accommodate them. On the eve of the first world war, textiles made up no less than 51% of British manufactured exports. Whereas previously they had gone to Europe, they now went to the Empire. The Asian colonial market absorbed anything up to 60% of these exports in the years before the first world war. As Eric Hobsbawm has put it, "Asia saved Lancashire". But it did more than that: by keeping Lancashire afloat it sustained demand in the UK market for exports from the rest of the world, thus easing tensions within the core. Even more important, India indirectly sustained the international monetary system of the day. If the Indian market had closed and Lancashire had collapsed, the pressures, already growing within the UK industrial heartland in the early 20th century,[69] for protectionism would have been unstoppable. If the UK had opted for protectionism, the international monetary system would have been scrapped.

[68] These began with the construction of 'European Political Co-operation' and the project of monetary union by 1980, both launched at the start of the decade. Though both were largely abortive, the impulses behind them remained, and gathered strength.

[69] These pressures were championed by Jo Chamberlain, the political leader of the West Midlands industrial bourgeoisie.

An analogous system has developed in the context of the core stagnation of the last quarter of a century. The US has sought to use the dependent support regions as dumping grounds for US products through both an export drive and market-seeking FDI. It has used the IMF and the dynamics of the Dollar-Wall Street Regime to open up these states to restructure their international social relations of production to ensure that they could absorb these products. The resulting substantial increase in US exports has, in turn, sustained the US domestic product market, easing tensions in the core. In a similar pattern to the British case, over half US exports in the 1990s went to countries of the South, not least Latin America. Yet even in its own Latin American hinterland, the US exported less than did the EU.And both in the earlier period and the current one, the dependent support-regions were very important sources of cheap, vital inputs into the productive processes of the core states.[70]

There is, of course, an important difference between American and British control mechanisms over the dependent support regions: British direct imperial rule meant there was no balance of payments constraint on the colonies since their monetary system was Sterling. The British could have them running permanent deficits with the metropolis without having to provide them with a market to cover their deficit-induced debts. For the United States, using the dollar-Wall Street regime there is a constant need to provide the dependencies with a sufficient export market to cover debt servicing to the US financial sector. On the other hand, the British had to take direct responsibility for maintaining order in their dependencies, while the US system throws that responsibility onto the legally sovereign dependent state. So it is a case, probably of swings and roundabouts, even though the function of being 'market of last resort' may seem a heavy burden for the US.

But as Patnaik has shown in his masterly and seminal study [71], there was another actor in the world economy outside the core at the end of the 19th century whose role was also integral to the dynamics of the system as a whole. This other kind of actor was made up of the states which could be called the new growth centres. These could absorb surplus capital from the core as well as surplus labour for the purposes of productive capital accumulation. Between 1865 and 1914 the bulk of capital exports from the core took the form of British portfolio investments. And during that period as much as 68% of total British portfolio investment went to the new growth regions, some juridically within the British Empire, others outside it.[72] This outpouring of funds from British rentiers to the new growth centres was itself a

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[70] Although now intellectually discredited by the work of Walter and others, the American theory of so called hegemonic stability which argues that the world needs one overwhelmingly dominant state if there is to be stability in the world economy (and especially its monetary system) , had the great merit of pointing to the lack of automatic stabilisers in the core economy. Their question: who will provide the 'public goods' of stability is best answered by saying it is provided by the dependent support-countries of the South, even though the goods they provide are not really 'public' since they are enjoyed only by the core economies. On the theory, see Walter: World Power and World Money (Harvester).

[71] Prabhat Patnaik: Accumulation and Stability Under Capitalism (Clarendon Press, Oxford, 1997).

[72] Estimates by Matthew Simon, cited by Patnaik in Prabhat Patnaik: Accumulation

shift from their earlier destination towards the more backward West European core.

The same kind of pattern has occurred in the later period, though with significant modifications. In the first place, stagnation in the core has not enjoyed the safety valve of huge labour migrations outwards. And in the second place the outflows of funds from the core for productive investment in the new growth centres has come not only from rentiers in the lead country, but from productive capital in the rest of the core as well.

Another parallel is also important: in both periods, organised labour and the socialist movement seemed very weak and as a result strategies could be adopted for displacing tensions between the core countries not only towards the hinterland but also onto the working class (with labour emigration making this especially easy in the earlier period). Similarly, by the 1990s, it was hoped that labour was so permanently weakened by the collapse of the Soviet Bloc that tensions could largely be displaced downwards via so-called neoliberalism.

Of course, there are important differences between the two periods as well. The internationalisation of finance out of London was more extensive and deeper in the earlier period than in has been in the current period. British banks alone had over 8,000 branches around the world. Secondly, the juridical empire form of external expansion is no long viable: direct control of populations in the South can no longer be sustained by imperial centres: institutions like the IMF, the WTO, bilateral security Pacts and multinational companies must be used in combination with juridically sovereign states which are then required by the imperial system, as well as by international law to shoulder exclusive responsibility within their territory for whatever the results of interacting with the core economies may be.

Thirdly, the internationalisation in the earlier period took place in a context of extraordinary stability of the international monetary and financial system of the core, unlike the chaos of the dollar-Wall Street regime.

But the big question for historically-minded American policy makers in the 1990s has been whether there would be two more parallels between the earlier period and the current one: first, in the earlier period, a challenge to British power came from within the core in the form of the First World War; Britain survived this challenge, but fatally weakened as a dominant power in monetary and financial relations. Could a similar kind of challenge face the US? But secondly, Britain faced a different kind of challenge from the new growth centres. The countries in this group included such dominions as Canada, Australia and new Zealand as well as other states such as Argentina, Japan *and the USA*. The USA took the exported funds from the core and seized control from Britain through helping it cope with its challengers in the European core. Could this happen again in, of course, a novel form?

It was not too difficult to perceive actors which could reproduce for the United States both these kinds of challenge that had faced Britain: the first could be described as the monetary-financial threat; the second, the new productive centre threat:

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and Stability Under Capitalism (Clarendon Press, Oxford, 1997)

1. The Financial-Monetary challenge: this challenge could arise above all from the combination of the construction of the Euro with financial instability within the United States itself. A serious American financial crisis could turn the dollar-Wall Street regime into its opposite: there could be a flight from US Treasury bonds, prompting a flight from the dollar feeding back into a really serious US foreign debt crisis: if something happened to produce a drying up of US financial markets for foreign borrowers, the latter might dump the Treasury bonds they had been using as a safe haven for their dollar reserves. There could be a double effect: the costs of servicing the US debt in the dollar market for Treasury bonds would soar, as interest rates shot up; at the same time interest rates in Europe fall as people dump dollars for Marks (or Euros). The US has to service its debt by borrowing in Marks and Yen, yet has a current account deficit with both these currency zones. At this point, people begin to worry about the medium-term future of the dollar, and the gigantic mass of greenbacks now masses all over the world after a quarter of a century of the Dollar-Wall Street system would give the crisis a new quality as people all over the world started to flee this dollar overhang: in such a situation the dollar could begin to resemble the ruble -- a currency whose fall seemed to have no floor. This, of course, was a nightmare scenario, imaginable only in the event of a collapse of the American financial system of Mexican proportions. Yet the same results could occur over a longer period in a series of fairly small, incremental jolts. And the end result would be the same in either case: American policy makers would wake up one day to face the inescapable fact that world leadership had passed elsewhere.

This trend could, of course, only occur if there was an obvious alternative global currency to the dollar. Such an alternative could not be the yen, because despite the unmatched size of Japan’s financial surpluses, its domestic financial market is far too small to support the yen as a world currency and the Japanese economy is rather closed in trade terms -- its exports and imports are a small proportion of its GDP. But the Euro could be a very different matter. It could quickly establish itself as a major international currency, backed by large current account surpluses and large capital exports. And if its financial markets were integrated, they could quickly rival Wall Street as sources of international finance. Were the EU then to adopt tough interpretations of its laws on reciprocity in rights for foreign financial services operating within the EU, it could curtail the operations of US banks and other financial operators within the EU until its operators gained equal scope in the US market (which they do not have at present). This prospect is, to put it mildly, an uncomfortable one for any US government.

2. The New Productive Centre Threat: This was a seemingly less urgent threat, but a more dangerous one. It would arise from the symbiosis of Japanese capitalism with the growth centre of East and South East Asia as both become the centre of gravity of the global production system, making the profitability of American capital dependent upon its links with the region, while simultaneously reorganising the international division of labour in such as way as to place US industry in a subordinate position: the high prestige ‘positional goods’ -- the high status products for the international wealthy classes -- and the fixed capital to produce them would be East Asian. This threat could materialise with special force in the event that a ring was thrown around Japan and the region in the form of a yen-zone come trade bloc along West European lines. Suddenly the US could find itself faced with collective resistance to its efforts to use its political muscle to break into strong positions in the region. The DWSR would be crippled by the yen zone as a source of leverage while Japan, not a debtor country, would be generating huge financial resources for productive investment.

And the finance ministers of the South and even from the US would be queuing in Tokyo for investment and financial support, while the offices of the IMF and World Bank would be occupied only with a dwindling band of exclusive US dependencies. And the Japanese regional leaders could be happy to help the United States solve all its problems of managing its decline, as the US had been with Britain earlier in the century: they could even prop up a Dollar-Wall Street area analogous to the Sterling-City of London area propped up by the US in the post-war years.

Both these potential threats have been central pre-occupations of US policy intellectuals since the late 1980s. Of course, they were not the only topics of discussion. The US had huge political resources for combatting them and for reshaping the post-Cold War world in ways that would entrench the US as the dominant power throughout the next century. And since the US has the lowest tax rates in the advanced capitalist world, it could take the needed structural measures -- a sharp increase in the share of taxation in GDP, to put its state finances on a sounder footing.

But the level of policy analysis and debate as the Clinton Administration came into office was qualitatively different from the past: the issues to be addressed were no longer those of incremental tactical adjustment within a largely given strategic environment. Fundamental, historical strategic review was on the agenda.

Of the two threats, the EU one looks superficially more menacing. Yet there were counter-balancing factors. First, the threat from the Euro did not come from its creation, but from its being able to challenge the dollar as a world currency. Such a challenge would require a number of supports which the EU was unlikely to acquire quickly: a solid political base that could be counted upon to act as a single political unit in a crisis; a major military-political capability autonomous from the US, something on which there were few signs of progress; a unified and powerful financial sector, buttressed by a unified political authority -- something a long way off; a coherent and politically acceptable domestic Euro-land economic and social policy framework, something which spontaneous market forces would tend to undermine; a means of exiting the long European stagnation, something that the ECB was hardly likely to produce; a means of ending the politically disintegrative tendencies within Euro-land politics, witness by the growth of the extreme right and the deep splits on social policy and EU-wide democratic identity; perhaps most crippling, there was the patchwork of torn or shattered social and economic structures in the Eastern part of the continent and the evident incapacity of the Euroland states to even begin to offer a coherent, serious answer to these problems. And finally, West European leaders had such endless capacity to bicker among themselves that it did not take much on the part of a US administration to throw them into sixes and sevens. Meanwhile, US capital not only had very easy access into the EU market and the existing EU political structure was an extremely favourable one for US operators since at its heart was a Commission uncontrolled by EU internal democratic mechanisms, fixated on one problematic -- deregulation to assist transnational business -- and therefore easily captured by the influence of US transnational corporations.

The East and South East Asian region seemed at first sight to be less menacing because of its political fragmentation. Yet there were two sets of powerful and potentially complementary social networks tying the regions capitals together: the networks centring on Japanese business and the networks linking overseas Chinese business with the mainland. And these two networks were creating growing linkages and complementarities in the one region of the world with really dynamic accumulation. Furthermore, the networks were tending to leave US capitals out. Worse still, the more advanced economies were directly eating into markets of core US capitalist sectors. And the region was becoming increasingly organic with Japanese capitalism. And in most of the countries there were barriers of various kinds to the US being able to establish its predominant influence within their political economies.

While from the angle of mainstream economics, the Clinton administration faced no political-economy threat at all. From the angle of neo-mercantilism, threats would be visible everywhere. But from the angle of our hypotheses, the direction of the threat for the Clinton Administration, would be from East and South East Asia. And it was potentially a very serious one because rooted in dynamic capital accumulation which was showing every sign of moving up the hierarchical international division of labour. Of course, there were incentives for US capitalism to swim with the spontaneous tide, since it was making large absolute gains in terms of exports, intra-structure investments etc. But this was also a kind of danger since the more these absolute gains loomed large, they would make it more difficult for the American state to take tough action to prevail over the regional challenge.

B. The Strategy of the Clinton Administration

The Clinton Team and its General Stance

The atmosphere in the United States when Clinton came into power was one suffused with a sense of great historical drama, a sense that the United States was facing a great world-historical Either/Or. There was the awareness of America's gigantic power in the military field and in the monetary-financial regime; on the other hand, there was the challenge of East Asia and uncertainty about Europe. There was the sense that the United States was about to give birth to an entirely new set of global growth motors through the new information industries and a feeling that these could play the role of the motor car as a huge pathway to revived international accumulation which the US could hope to dominate; yet after very large investments in this sector its supposed transformative potential for US productivity has simply not materialised. And finally there was the triumph over the Soviet Bloc and the international left; and yet paradoxically that collapse posed a major question-mark over the means that the US could use for exerting political influence in the world and consolidating that influence through institutions similar to the security zones of the Cold War.

Tremendous American intellectual energy was being devoted, therefore, to these strategic issues as Clinton came into office. As one policy intellectual put it, "essentially, we have to erect a whole new conceptual basis for foreign policy after the Cold War"[73]. Others equated the tasks facing Clinton to those that faced Truman in 1945: Clinton, said one writer, is 'present at the creation' of a new epoch in world affairs and 'the next half century hangs in the balance'.[74]

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[73] Will Marshall, head of the Progressive Policy Institute, Washington Post, 21st December,1992.

[74] Roger Morris, "A New Foreign Policy for a New Era", New York Times, 9th December,1992.

The Clinton team itself was not, of course, going to spell out publicly how it conceptualised its strategic problem and its strategy and tactics for tackling it. The signs had to be read more indirectly, for example, through Clinton's appointments and institutional arrangements as well as through its policy statements and initiatives.

Clinton's top foreign policy appointments, like Warren Christopher (State), Anthony Lake (National Security) Madeleine Albright (UN), Lloyd Bensten (Treasury) were conventional, rather passive figures with links back to the Carter days.[75] Many observers wondered why Clinton had received a reputation for external activism when he made such personnel appointments.[76] But this perception was itself the product of old thinking whereby foreign policy meant what the Secretary of State or the NSC chief or the Secretary of Defence did. It ignored the instruments of economic statecraft, yet these were the instruments which Clinton placed in the hands of the dynamic activists.

The new team brought in to wield the levers of economic statecraft were a distinctive group: Robert Rubin, Ron Brown, Mickey Kantor, Laura Tyson, Larry Summers, Jeff Garten, Ira Magaziner and Robert Reich (as well as Vice President Al Gore) had distinctive general approaches to the defence of American power[77]: For them, it was about 'the economy, stupid'. And they believed that strengthening American capitalism was above all to be tackled through international political action. In line with this was their belief in the importance, even the centrality of state political action in economic affairs: a conviction that the success of a national capitalism was 'path dependent' and the path could be built of institutions fashioned by states. And there should not be barren counter-positions of national states and market forces: they should work together, help each other, whether in technology, trade or finance. They were not classical national protectionists, but they were also not free traders. The term used to describe the school of thought represented by this team was 'globalists', promoters of a kind of global neo-mercantilism. The new concept was that competition among states was shifting from the domain of political-military resources and relations to the field of control of sophisticated technologies and the domination of markets.[78] The nature of the new game was also given a name: 'geoeconomics'. Lloyd Bensten may

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[75] Aspen in Defence had a more activist, radical agenda.

[76] See, for example, Anthony Hartley:"The Clinton Approach: Idealism and Prudence", The World Today, February,1993.

[77] Of this list one partial dissident was Robert Reich: he shared a belief in state action in international economics and his concern for labour standards and protection could be usefully instrumentalised in economic diplomacy over trade issues. But he lacked some of the America-First-in-Everything zeal of the others and dropped out of the administration eventually.

[78] Gioia Marini and Jan Rood: 'Maintaining Global Dominance: the United States as a European and Asian Power.' in Marianne van Leeuwen and Auke Venema (eds.):Selective Engagement. American Foreign Policy at the Turn of the Century.(Netherlands Atlantic Commission, The Hague, 1996)

have been of a different generation and of a different background from the others, but he also shared a ‘globalist’ view.

The outlook of this new team was expressed in books like Laura Tyson’s “Who’s Bashing Whom” and by a host of other such works by those within or close to the administration.[79] The outlook was often expressed most bluntly by Clinton’s new US Trade Representative, Mickey Kantor, who openly argued for a new kind of American Open Door strategy to ensure that the 21st Century will be the ‘New American Century’. As he put it: “The days of the Cold War, when we sometimes looked the other way when our trading partners failed to live up to their obligations, are over. National security and our national economic security cannot be separated....No more something for nothing, no more free riders.”[80]

Kantor’s linkage of external economic objectives and US National Security was reflected in Clinton’s remoulding of institutions in the core executive: just after Clinton’s inauguration he created a National Economic Council within the White House alongside the National Security Council . The choice of name was designed to indicate that the new body would acquire the kind of nodal role in US global strategy which the NSC had played during the Cold War. At the same time Congress instructed the Commerce Department to set up the Trade Promotion Coordinating Committee (TPCC) to co-ordinate 19 US govt agencies in the area of commercial policy. Instructive also was the fact that the head of the National Economic Council was to be a very experienced hedge fund speculator, Robert Rubin, former senior partner in Goldman Sachs, the hedge fund masquerading as an investment bank.[81] This gave the Clinton team prime links with Wall Street.

The way that the Clinton Administration defined its approach has been summed up by someone who was initially part of it, David Rothkopf. He has characterised the Clinton administration’s new international strategy as one of “Manic Mercantilism”[82]. Stanley Hoffman makes a similar point, noting the new US activism in world economic affairs under the Clinton administration and its drive to open borders to US goods, capital and services.[83].

The Strategic Focus on East and South East Asia

It has been widely suggested throughout the Clinton Presidency by many attentive observers

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[79] See Laura D’Andrea Tyson: Who’s Bashing Whom: Trade Conflict in High-Technology Industries (Institute for International Economics, Washington DC,1992); Ira Magaziner and Mark Patinkin: The Silent War: Inside the Global Business Battles Shaping America’s Future (Vintage Books,1990); Jeffrey E. Garten, A Cold peace: America, Japan, Germany and the Struggle for Supremacy (New York Times Books,1992)

[80] USIS, February 23rd 1996: “Kantor says US to Fight Farm Trade Barriers.”

[81] Rubin later was to become Treasury Secretary -- his current position.

[82] David J. Rothkopf: ‘Beyond Manic Mercantilism’. Council on Foreign Relations, 1998.

[83] Stanley Hoffman, Martin Wight Memorial Lecture, LSE, June 1998.

that its efforts in economic statecraft have been mainly directed at one particular geographical area: East and South East Asia. Rothkopf suggests this was the main motive for the entire drive, saying: “Commercial diplomacy, however defined and practised, owes its development as much to the rise of Asia’s emerging economies as it does to any other factor.” East and South East Asia were of decisive importance if the United States “ was to maintain its economic leadership.”[84]

[84] Rothkopf, op. Cit.

The Clinton administration never admitted quite this, of course. It claimed instead that its target was to break into what it called the 10 Big Emerging Markets (BEMs): but 6 of the ten were in Asia: China, Indonesia, Korea, Thailand, Malaysia and India. Of the other four, the United States already had two: Mexico and Argentina. A ninth, Poland, actually fought its way onto the administration's list. That left only Brazil outside Asia as a major target of American interest. So basically, the list of BEM targets meant Asia. The Clinton administration targeted $1.5 trillion to $2trillion of commercial opportunities in the world's emerging markets with $1trillion in export opportunity targets. According to Rothkopf US "intelligence agencies were drawn into the commercial fray, providing analysis and other forms of assistance for these efforts."[85]

The BEM strategy was first outlined by Undersecretary of Commerce for International Trade Jeff Garten in a January 1994 speech to the Foreign Policy Association in New York. John Stremlau, Deputy Director of Policy Planning at the State Department,1989-94, pointed out that although it appeared unusual for Clinton to define his "foreign policy doctrine in terms of special US interests in a limited number of key countries" Reagan had largely done so by targetting Afghanistan, Angola, Cambodia and Nicaragua. Stremlau pointed out that Indonesia had been singled out for special attention, not least because there the US was losing market share to the Japanese and the Europeans. He also explained that the US drive into Indonesia "could complicate US relations with Japan, which views Indonesia as lying within its sphere of influence." The key word was to bring about economic and political 'convergence' between the United States and the targeted states: in other words transforming the domestic economics and politics of these states to achieve a kind of gleichschaltung between them and US capitalism. As Stremlau put it: "Clinton administration strategists seem to have concluded that domestic imperatives and international realities require a new and more subtle version of 'dollar diplomacy' -- greater US economic and political convergence with the few countries that make up today's Big Emerging Markets. Success on all those diplomatic fronts is as daunting a foreign policy goal as any in the country's history, but success could lead to a century of unsurpassed prosperity and security for the United States..."[86]

The Clinton administration openly called for a partnership with US business to break into these markets and Commerce Secretary Ron Brown, directly urged US companies to seek political help from the Administration *on particular contracts*. In addition the Ex-Im Bank, OPIC and the Trade Development Agency was geared up for providing priority assistance to US companies seeking entry and domination in markets in the BEMs.

But this could only be a minor detail. According to a study conducted by the Dutch section of the international association of Atlantic Councils (the civilian opinion-forming arm of NATO), the Clinton administration's key concept in its external economic strategy was that competition among states was shifting from the centrality of political-military resources to the field of control of sophisticated technologies and the domination of markets.[87] This view

[85] David J.Rothkopf: "Beyond Manic Mercantilism" Council on Foreign Relations.

[86] John Stremlau: "Clinton's Dollar Diplomacy", Foreign Policy, 97, Winter 1994-95.

[87] Gioia Marini and Jan Rood: 'Maintaining Global Dominance: the United States as

closely corresponds to our hypothesis as to the rational external strategy for the US in the 1990s, directed towards East and South East Asia. The big problem was what mix of tactics the US could deploy to decisively open the region up to US hegemony.

Tactical Options

We can outline some options available to a state with the resources of the USA for bringing the pools of labour and markets of the region permanently under the sway of the US and its economic operators.

1. The old European imperial power approach: direct military coercion and subordination.
2. Brigading the states of the region into a US-led alliance against some external threat: the classic post-war US approach to gaining hegemony over key centres of production.
3. Launching all-round economic warfare against the region (including oil-war like that used by the Nixon administration against its 'allies' in the early 1970s).
4. A more radical, activist strategic use of the multilateral organisations.
5. Using a mix of carrots and sticks in bilateral and regional economic statecraft.
6. Seeking domestic social linkages in target states through propaganda.
7. Using the instruments available through the DWSR for currency and financial warfare.

We will briefly survey each of these possible instruments in order to gain some insight into the tactical dilemmas of the Clinton administration.

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a European and Asian Power.' in Marianne van Leeuwen and Auke Venema (eds.):Selective Engagement. American Foreign Policy at the Turn of the Century.(Netherlands Atlantic Commission, The Hague, 1996)

1. Direct military coercion and subordination: This, of course, was not a serious option, but it is instructive to see why not. Quite simply, despite the enormous advances in weapons technology and the overwhelming superiority of US military capacity direct military coercion followed by effective colonial subordination is unthinkable in today's world. The first reason is that as the US military's capacity to kill rises towards infinity, its capacity to die sinks towards zero. And to directly control populations and deal with popular movements in the contemporary world requires that military forces have a substantial capacity to die.[88] The rise of the world's population to political awareness and their acquisition of some free time rules out the old 19th century tactics of the gun-boat and colonialism. The alternative course is to achieve ascendancy through staging domestic political coups in order to impose dependent groups in power who will serve US business interests. But such activity cannot be conjured out of the air: it usually requires the existence of a perceived domestic threat (traditionally from the left) which the government of the day is perceived by a group within the dominant class as failing to deal with. Such preconditions did not exist in a region enjoying unparalleled economic advance and faced by no significant domestic social threats.

Yet if both these tactics are unavailable, there seems to be an irresolvable dilemma: given that state sovereignty has to be accepted, the US has not choice but to achieve its goals within these states *through* the existing dominant social class within these states. The problem thus becomes one of how to change the orientation of these dominant social groups.

[88] The deaths of 20 US soldiers in Somalia was enough to abort the US mission there. In the Bosnian and Kosovo cases, the Clinton administration was not prepared to put the feet of US soldiers on the ground while fighting was going on. Air power can destroy states but cannot control populations.

2. Brigading states into a US-led alliance against some external threat so that in exchange for US protection the states concerned open their economic assets to US operators: This is the classic US tactic of the Cold War period. Samuel Huntington has explained how US tactics worked: “Western Europe, Latin America, East Asia, and much of South Asia, the Middle East and Africa fell within what was euphemistically referred to as ‘the Free World’, and what was, in fact, a security zone. The governments within this zone found it in their interest: a) to accept an explicit or implicit guarantee by Washington of the independence of their country and, in some cases, the authority of the government; b) to permit access to their country to a variety of US governmental and non-governmental organisations pursuing goals which those organisations considered important....The great bulk of the countries of Europe and the Third World....found the advantages of transnational access to outweigh the costs of attempting to stop it.”[89]

And as David Rothkopf has added, in the post-war years “Pax Americana came with an implicit price tag to nations that accepted the US security umbrella. If a country depended on the United States for security protection, it dealt with the United States on trade and commercial matters.”[90]
The efficacy of the tactic depended upon two conditions: first, the ability of the US to persuade the local dominant social groups that they faced an external threat; and secondly, the US’s ability to persuade these same groups that the US and only the US had the resources to cope with the threat and the will to do so. In Western Europe the threat was, of course, the internal-external one of Communism and the dominant classes of the region needed little persuasion -- on the contrary they were in many cases begging for US intervention.[91] The distinctive US organisational model of the giant corporation could thus enter foreign labour and product markets, spreading first to Canada then to Western Europe (facilitated by the EC’s rules and development) and then on to other parts of the world. In this way, rather than in the primitive militarist conceptions of realist theory, military power played a central role in post-war capitalist power politics.

With the collapse of the Soviet Bloc, the Bush administration had still hoped that the United States role as controller of security zones and wielder of enormous military resources could remain a potent instrument for strengthening the position of American capitalism vis a vis its economic rivals. His great efforts to ensure that a united Germany remained in NATO were followed by his war against Iraq, one of whose main goals was to show the rest of the capital world that it had to treat the interests of US capitalism with respect. But this was a false dawn. With the collapse of the Soviet Union itself, the US’s ability to make political use of its extraordinary military superiority was bound to diminish.

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[89] Samuel P. Huntington, ‘Transnational Organisations in World Politics’ World Politics, Vol.25, No.3 (1973) p.344.

[90] David J.Rothkopf: “Beyond Manic Mercantilism” Council on Foreign Relations.

[91] For the British, the threat came within their Empire (and indeed, partly from the USA’s desire to open it up). But by getting the US to take over the battle against Communism in Europe, they hoped to free their own resources to save the Empire against a whole range of pressures, including American ones.

It has not, of course, disappeared. The fact that the US has military resources today greater than all of Western Europe, China, Japan and Russia put together is a fundamental fact about world politics. It is evidently determined to retain the capacity to fight and prevail in a war against the combined forces of Russia and China.[92] This is not, of course, because it wishes a war with these two states. But if these two states did form an alliance in hostility to the capitalist world, the US could cash its strategic military power again politically, by being able to brigade the rest of the core more firmly under its influence. And this military power also has another very important function: it can deter its 'allies' from making international political alliances which might threaten US capitalism. When Germany and other parts of Western Europe seemed, in the late 1970s to be moving towards a new regime of deepening economic co-operation with the Soviet Bloc (in the face of the economic stagnation and the chaotic conditions of the DWSR at the time), the US had been able to cut the movement dead with its battle cry against the 'Finlandisation' of Western Europe, with its missile deployments in Germany and Italy and with its general offensive in the second Cold War. This, in itself, rules out either of the two other triadic centres even contemplating mounting a direct challenge to American leadership of world capitalism. Neither Germany nor Japan has shown the slightest hint of an interest in such an adventure.

But the problem for the US has not been stopping the other triadic powers from mounting a direct political challenge. The problem has been losing political leverage to secure its economic interests within their new, post-Cold War hinterlands: East Central and Eastern Europe and East and South East Asia. Insofar as such regions face no external threat whose tackling requires military resources such as only the US can supply, the instrument of Cold War diplomacy lose their efficacy.[93]

In 1993 the Clinton administration did attempt to use this Cold War style diplomacy in East Asia through using a double barrelled approach. It simultaneously raised two threats: first, the supposed danger to the region of a North Korean nuclear strike; and secondly, a lower-level kind of 'threat' -- China's human rights behaviour.[94] Both, of course, had an anti-communist flavouring. These demarches were coupled with a drive to brigade the non-Communist East and South East Asian countries, including Japan, into a major drive to open their economies to the US within the so-called Asia Pacific Economic Co-operation (APEC), the aim of which was both to open up the economies of the region in ways which

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[92] See Gilbert Achar: New Left Review..

[93] Of course, great powers do not simply have to *respond* to locally created dangers and crises. They can *create* local crises and threats which then lead other states in the vicinity of the crises to welcome or at least accept the great power's intervention to tackle the crisis. Those who have followed attentively the Bush administration's operations in relation to Bosnia in 1992 can see the unmistakable signs of the US deploying such tactics in the EU's hinterland. See Susan Woodward: The Balkan Tragedy (Brookings, 1996).

[94] This campaign dove-tailed, of course, with the British campaign to keep Hong Kong's wealth-stream flowing in the right direction after the hand-over of the colony to China.

favoured US penetration and to weaken the impulses towards regional economic co-operation within ASEAN to the exclusion of the USA.[95]

[95] On US perceptions of ASEAN in the early 1990s as the embryo of a move towards a Japanese regional bloc, see C.Michael Aho: "America and the Pacific Century: Trade Conflict or Co-operation?" International Affairs, 69, 1, 1993.

But these efforts to use the old Cold War techniques for economic objectives failed. The confrontation with North Korea misfired as the US discovered that Pyongyang could be pushed into actual military conflict as a result of fear of an American strike -- and military conflict was actually the last thing the US wanted -- while the US simultaneously found that other states in the region preferred *Chinese* mediation *between* Pyongyang and Washington to lining up behind US bluster against North Korea. It was a diplomatic disaster and humiliation for the US. As for the attempt to mobilise political support in the region for an alliance against China based on Human Rights rhetoric, this overlooked the fact that most of the potential allied governments found US rhetoric about Human Rights distasteful, at best. After declaring early in 1993 that continuing US-Chinese trade relations would depend upon improvements in China's respect for Human Rights,[96] the Clinton administration felt compelled to declare a year later that "we need to place out relationship into a larger and more productive framework" than one centred upon Human Rights.[97] This change of line came at a time when Washington needed Peking's help over North Korea. But it also came after a year in which Washington's European allies had refused to follow Washington's lead on the Human Rights card and were eager to gain as much extra business in China as possible.[98]

3. Launching or threatening all-round economic warfare against the region (including oil-war, like that used by the Nixon administration against its 'allies' in the early 1970s): This idea has been intensively and publicly aired within the United States in relation to Japan since the mid-1980s. The seriousness of this was demonstrated by the way in which a public media campaign to identify Japan as an enemy and a threat was developed by some influential groups within the United States. Yet a direct, frontal campaign of economic warfare and blockade against the whole region or against Japan would have been enormously costly and counter-productive. The European powers would probably not have co-operated. The campaign could have destroyed the tissue of US-led international institutions and could have destabilised the American economy itself. Instead, the concept of all-round economic warfare was deployed by the Clinton administration as a threat, a potentiality, supported by the assembling of a battery of instruments and operational concepts. These instruments included mechanisms such as the Super-301 instrument for unilateral trade-war, created in the Reagan period, the strengthening of so-called anti-dumping actions, the declaration that US economic access to other economies was now a *national security issue* (thus an issue on which economic warfare could be used), and the doctrine of the existence of *economic adversary states* to which liberal economic principles should not be applied. Alongside these concepts, the Clinton administration dropped even lip-service to so-called GATT multilateral principles in trade issues, adopting instead as its key principle reciprocity and raising the slogan of 'fair' trade. And finally the threat that the US would build a regional fortress in the American hemisphere which would be used to exclude East Asian operators.
4. An activist drive to change the programmes of the multilateral organisations.

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[96] David Lampton: "America's China Policy in the Age of the Finance Minister:Clinton Ends Linkage", The China Quarterly, No.139 (September 1994).

[97] Press Conference statement, The White House, 26th May,1994.

[98] Lampton, op.cit.

Within the workings of the DWSR, US administrations in the 1980s had extracted gains from crisis-hit countries in terms of opening their financial markets to free flows of international funds, opening their financial markets to US financial operators, opening their asset markets for buy-out by US corporations and so on. But these were piecemeal gains associated with particular countries and crises. Some of them, particularly in relation to the free flow of international funds were partially reversed, as occurred in Chile and other places. But the problem was that East and South East Asia had largely escaped such treatment because these states had largely avoided financial crises.

Building upon work already achieved under the Reagan and Bush administrations, the Clinton administration decided to radicalise the programmes of various multilateral organisations in order to commit them to the radical opening of national economies. This would then turn them into the functional equivalent of the role played by what Huntington called the security zones of the Cold War. States that wished to function within these multilateral institutions would, to paraphrase what Rothkopf said in the context of bodies like NATO, have to deal with the United States -- the controlling power within these organisations -- on its domestic economic assets. And if the state tried to evade 'dealing with the United States' on these issues, it could be excluded from members of the multilateral institutions. And if it was so-excluded, it could be subjected to a full range of instruments of economic warfare and be denied secure insertion in international markets, since such secure insertion increasingly depends upon a state's good standing in the multilateral organisations. The result was four inter-linked campaigns to change the programmes of these bodies as follows:

1. first, changing the programme of the IMF to commit it to the ultimate complete dismantling of controls on the capital account in every country, letting funds flow into and out of countries freely. The great political triumph on this was the decision at the IMF/WB gatherings in Hong Kong in 1997 to change the IMF Articles of Agreement to commit it to complete liberalisation in this way.
2. second, adding a new programmatic package to the World Trade Organisation's programme through an agreement to liberalise financial services with the ultimate objective of complete freedom for financial operators to enter every financial system with the same rights as local operators (so called national treatment). The great political triumph here was, supposedly, the deal achieved in the World Trade Organisation in December 1997 on the global liberalisation of financial services;[99]
3. third, changing the programme of the OECD in two main ways: first making the ending of controls on capital accounts and on the movement of financial service operators a precondition for OECD membership; and second through adding a package of rules known as the Multilateral Agreement on Investment (MAI) which would grant complete freedom for industrial corporations to move into national economies and buy up local companies, set up their own operations and dominate local product markets: the great political triumph here was supposed to occur in 1998, with the final MAI agreement, although the OECD horse would, as it turned out, stumble at the last fence in the negotiations.
4. fourthly, a whole battery of other measures, from the organisation of securities markets to

[99] The WTO Financial Services Agreement did not, in fact, go as far as the US had hoped. See Wendy Dobson and Pierre Jacquet: Financial Services Liberalisation in the WTO (Institute for International Economics,Washington DC, 1998)

the protection of technological monopolies (so called intellectual property rights), to be adopted by the multilateral organisations giving their (US) leadership the right to reorganise state's internal social relations of production to fit with the requirements of US operators, or, to put the point another way, to match the most recent scientific advances in economic thought as expressed by the Washington Consensus.

The point about these campaigns was not actually to tear down all the institutional barriers everywhere at one go. As a matter of fact, the Clinton administration would not necessarily have had the slightest objection to an ally like Chile re-imposing some element of capital controls. The point was to use these changes in the programmes of the multilateral organisations as what might be described as political can-openers to open the lids of *certain specific political economies:* those of East and South East Asia.

It is important to understand the exact politics involved in the radicalisation of the programmes of the multilateral organisations. First, the drive could appear to respond to the great power of the idea of establishing a cosmopolitan system of global governance for it responds to deep, wide and thoroughly justified human yearnings in the contemporary world to overcome nation-state rivalries. The programme radicalisation seems to achieve this. Secondly, there is the great power of the idea of replacing the command politics of one state against another by the rule of law, universal laws by which all will be bound. The radicalisation programme seems to correspond to this desire since people assume that the multilateral organisations work in a rule-based way. But thirdly and most crucially, these two powerful ideas co-exist with a reality which entirely contradicts them: the multilateral organisations are supranational forces for most of their member states but not for all, not for those states, above all the USA, which control them. An organisation used by one state to govern the globe is not a supranational institution of 'global governance' The US can block items it dislikes off the agendas of the IMF/WB and the OECD. It agreed to the WTO's creation on the explicit basis that if WTO rulings were 'unfair' to the US, then US governments would be duty bound to ignore them. And this leaves the WTO as a framework not of law but of bargaining. In cases where the US can strike a better deal bilaterally outside the framework of the WTO it will do so and will strike such deals in violation of WTO principles. And as the Dutch Atlantic Commission 's study of US trade policy shows, this policy was moving, under Clinton, under the code word 'fair trade', in the direction of managed trade, using the governing principle for the United States of reciprocity rather than multilateralism.[100] The concept of managed trade, systematically pursued by the US towards Japan, involves replacing a rule-based trade regime with a results-based regime. In other words, target states must accept certain quantitative targets for their imports and exports of particular sets of goods, as in Comecon-style trade planning.

[100] Examples of managed trade are the emphasis since the 1980s on the part of the EC and the US on so-called Voluntary Export Restraints(VERs) and the US emphasis, particularly in East Asia and Japan on Voluntary Import Expansion(VIEs). Both VERs and VIEs are 'results-oriented' instruments characteristic of managed trade. See Frank Buelens: US Trade Policy: Free Trade or Fair Trade' in M.van Leeuen and A. Venema (eds.):Selective Engagement. American Foreign Policy at the Turn of the Century (Netherlands Atlantic Commission, The Hague,1996).

But a final feature of the US politics of radicalising the programmes of the multilateral organisations should be noted. The entire drive could not have been accomplished without the support of the European Union and its member states. Following the conclusion of the Uruguay Round there were unmistakable signs of a new Atlantic Partnership for reorganising and resubordinating the world economy in the interests of these two centres. As US Assistant Commerce Secretary (for market access and compliance) Vargo has explained, "Experience has shown that, large as we are, we cannot open the global marketplace on our own. We must have partners in that endeavor....No trade round or other major multilateral initiative has been achieved without the joint leadership of the United States and Europe."[101] And Vargo goes on to explain how prior US-EU agreement was vital for the Uruguay Round, the Information Technology Agreement and the Basic Telecommunications Agreement. The same was also true of the WTO financial services agreement and, until the French government's revolt, over the OECD's draft MAI Treaty as well.. Stuart Eizenstat, Undersecretary of State for Economic, Business and Agricultural Affairs has also underlined the centrality of this co-operative effort, creating pressure on Asian and Latin American countries to fall into line.[102]

The institution which has played the central role in preparing the ground for such transatlantic coalition-building has been the so-called Transatlantic Business Dialogue (TABD), proposed at the conclusion of the Uruguay Round in December 1994 by US Commerce Secretary Ron Brown and established in a first meeting in Seville in November 1995. As Assistant Secretary of Commerce Vargo has noted, his department advanced the TABD concept because it believed that "given the enormous cross-investment by US and European firms in each others' markets, a single transatlantic business community already existed that could agree jointly on common solutions which would benefit both the US and European economies."[103] The TABD meets regularly before the twice-yearly US-EU summit meetings to feed proposals into these summits.

5. Using a mix of carrots and sticks in bilateral and regional economic statecraft.

By combining continuous manoeuvring between bilateral, intra regional, inter-regional and multilateral moves in a very sophisticated way the Clinton administration has sought to maximise its gains. At one moment it seems to move towards a drive for a new economic Monroe doctrine to take over Latin America, weaken MERCOSUR and threaten to exclude Japan and East Asia or even Europe. When fear runs high in other regions, it then offers peace with say, East Asia in exchange for a big access deal of the right sort there. Europe then panics that the US is constructing a bilateral monopoly with Japan and offers either a bilateral EU-US monopoly or a global multilateral deal. Such offers are then taken back to Asia and turned into another threat of a bilateral monopoly unless ASEAN deals. And so on.

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[101] Quoted in Robert D.Blackwill and Kristin Archick:EU-European Economic Relations and World Trade (Task Force on the Future of Transatlantic Relations, Council on Foreign Relations, April,1998

[102] Ibid.

[103] Testimony before the House Committee on International Relations, Subcommittee on International Economic Policy and Trade, Federal News Service, 10th September,1997.

The Clinton administration thus used the tactic of threatened exclusion with skill: it laid enormous early emphasis on the supposedly massive strategic significance of NAFTA, making the EU and the East Asian countries fear Clinton wanted a regional fortress from which to wage trade war. This was an ideal atmosphere in which Clinton could finally lock horns with the French over the Uruguay Round. At the same time the Franco-American marathon neatly crowded out all other countries' concerns over the proposed WTO treaty since there was simply no time to tackle such problems: Asian concerns could be ignored. And armed with the WTO deal, the Clinton administration then agreed with Congress that the US would reserve the right to ignore the WTO if it started treating the US 'unfairly'. In the context of this anxiety, Clinton made much play of making APEC a mighty lever for constructing a US- Japanese bloc, provided, of course, the East and South East Asians including Japan opened their economies up to the US.

The Open Door drive in East Asia was pressed by the Clinton Administration both bilaterally and through APEC.The APEC summit in Seattle in 1993 agreed to create "a community of Asia Pacific economies" and spurred the successful conclusion of the Uruguay Round in the GATT. APEC's Bogor Declaration in Indonesia the following year pledged "to achieve free and open trade and investment in the region" by 2010 for the industrial countries that make up 85 percent of APEC trade and by 2020 for the rest. The 1995 Osaka APEC summit adopted a so-called Action Agenda that sets out the principles, the menu of issues and the timetables through which APEC's political commitments would be translated into tangible results. The APEC leaders at Osaka pledged to start liberalization in January 1997. The November 1996 summit at Subic in the Philippines demonstrated that the governments of the region were far from unanimous on the need to translate their high principles into practical liberalisation measures. But as preparations for the November 1997 Vancouver summit got underway, the mouthpieces of American financial globalization interests were pressing more strongly than even for the open door. Fred Bergsten, for example, from the Institute of International Economics in Washington, was still insisting:“Liberalization and deregulation of financial services are essential to sustain economic development throughout the APEC region (as elsewhere).” Yet APEC's actual practical progress in the direction the Clinton Administration wanted was minimal, even trivial.

Washington took an exceptionally tough stance for the radical demolition of controls on the movement of financial services, but it did so in a carefully targeted way, threatening to pull out of a WTO agreement and build its own network of liberalised financial services markets unless certain specific countries greatly liberalised entry of financial services: namely Thailand, Indonesia and other East and South East Asian countries. At the same time, the Clinton administration ensured that the OECD committed itself to insisting any new members must first dismantle their capital controls or get a plan for their dismantling agreed and then used that as a weapon against Korea, which was seeking OECD entry.

The campaign to open up East Asia's financial sectors had begun in the 1980s, focused on capital account liberalisation and financial deregulation. During the 1980s, Korea removed many of its controls on capital outflows, including portfolio investment abroad, outward financial credits and bank deposits. But it retained many restrictions on various kinds of capital inflows, especially those resulting in debt obligations. Up to 1997 ceilings were placed on total amounts of domestic securities that could be issued abroad. There were also ceilings on levels of portfolio investments in Korean stocks. But foreign investors were given easier access to domestic bond markets. And before Korea's accession to the OECD in December 1996, it removed a number of restrictions, such as those on intra-company loans of an FDI character, and those on friendly mergers between foreign and Korean companies (though mergers of the biggest Chaebols with foreign partners were still prohibited). By joining the OECD, Korea was obliged to design a schedule for implementing the OECD Codes of Liberalisation of Capital Movements and Current Invisible Operations and to endorse the 1976 OECD Declaration on International Investment and Multinational Enterprises as well as the OECD's 'National Treatment' Decision. Another important dimension is the relaxation of restrictions on cross-border trade in financial services. The liberalisation schedule which Korea agreed with the OECD involved speeding up liberalisation measures to complete most of them by December 1998 and the remainder by December 1999.[104]

While repeated US attempts to engage in trade conflict with Japan had proved increasingly ineffective because of the Japanese capacity to resist and even retaliate, Washington was able to wage a vigorous trade war against Korea: it imposed anti-dumping actions against Korean TVS, imposed so-called 'voluntary export restraints' on Korean steel, textiles and clothing, used the Super 301 clause against Korean products because it claimed Korea was using unfair practices and demanded great and greater opening of Korea to specific US products.[105] This waves of trade war against Korea worked. A Korean trade surplus with the USA of $9.6Bn in 1987 was turned into a trade deficit with the USA of over $4bn by 1996.[106]

Meanwhile both Thailand and Indonesia substantially removed their capital controls, but they did not open up full rights for US financial operators to compete in their domestic economies. Malaysia took a similar line. These countries' resistance to US operators gaining free entry and national treatment in their financial sectors was treated as a cardinal international issue by the US government at the start of 1997. It threatened to block the entire WTO package deal on the liberalisation of financial services unless Thailand and Indonesia in particular but other East Asian countries as well fully signed up to liberalisation. In the spring of 1997, the British government on behalf of West European governments sought to mediate and persuade the US government to moderate its demands. But for the Clinton administration, these countries were the key and the key to them was opening up their financial sectors. This was the position in April 1997 when a new actor entered the bargaining arena: the big US Hedge Funds began their attack on the Thai financial market.

But the aim of these kinds of attacks was not just a quantitative one. If so, by 1997 the USA should have been well satisfied: Korea had become the USA's fifth largest export market. The aim was a radical restructuring of the social relations of production within Korea in order

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[104] See Robert Ley and Pierre Poret: "The New OECD Members and Liberalisation", The OECD Observer, No.205, April/May 1997.

[105] See Walden Bello: "East Asia on the Eve of the Great Transformation", Review of International Political Economy,5,3,Autumn 1998.

[106] Ibid.

to engineer an economic gleichschaltung of Korean capitalism and of others in the region with the interests of American capitalism. And that required seeking internal allies within Korea and other states in the region, allies who could help to open the lid on their social relations.

6. Seeking domestic social linkages in target states through propaganda.

The Clinton administration's mercantilist trade diplomacy was simply, therefore, one tactical prong of a multi-pronged strategy. Another very important tactic was that of building and strengthening ideological linkages with strategic social groups inside the states of the region. At the level of mass propaganda, the key was the notion that all had to face the reality of an irresistible force whether for good or ill: the force was not, of course, the United States: if it had been, then it would have confronting the not insignificant force of Korean nationalism. No, the force in question was, of course, 'globalization'. But for a more sophisticated bourgeois audience a different kind of more focused propaganda campaign was launched, appealing to the rentier side of the passions of local capitalists. To appeal to this rentier interest, economic life is reconfigured as the constant struggle of the saver against brutal 'financial repression' for freedom to place his or her funds where s/he likes and for his or her right to a just royalty on a nest egg.

In the mid-1990s a large US propaganda campaign was targeted at the Korean business class's rentier inclinations by the institutions of the Washington consensus, including, not least the publications of the IMF and World Bank. A good example of such propaganda is provided by the Institute for International Economics in Washington, a tirelessly repetitive source of such transparently American-serving material. Their grandly titled APEC paper called ' Restructuring Korea's Financial Sector for Competitiveness' is a diatribe against 'financial repression' on behalf of the toiling Korean rentiers. It explains that without freedom " savers are offered low rates of return"; with financial repression "projects are typically not funded according to their rates of return, but rather on the basis of noneconomic considerations.....In the case of Korea, this is reflected in the low average rate of return on bank assets, which is among the lowest of those observed in emerging markets...More generally, government intervention in the financial markets erodes the autonomy of the private sector which becomes increasingly vulnerable to policy decisions by government officials....The result is income growth that is slower than needs be...." Furthermore " Markets cannot work efficiently in the absence of reliable information. Simply think of the problem of trying to value shares in the stock market under such conditions." and "Lastly, financial repression acts as an implicit tax on holders of government debt. By restricting capital flows, the government can in effect force domestic residents to accept government debt at lower interest rates than would be the case if there were no controls on capital."[107] In short, for the authors, economics is mainly about the human rights of savers to earn that extra percentage point of interest, a royalty cruelly repressed for decades by South Korea's malign concentration on economic growth.

7. Using the instruments available through the DWSR for currency and financial warfare[108].

[107] Institute for International Economics: Restructuring Korea's Financial Sector for Greater Competitiveness (APEC Working Paper 96-14)

[108] On the concept of financial warfare, see Michel Chossudovsky: Guerra

By 1997, it was possible to argue that the US had chalked up a significant range of quantitative successes in its East and South East Asian campaigns. It had achieved successes both in gaining new legal rights of entry and in gaining a greater quantity of profits from the region. Yet the relative weight of US capitals in the region's economy was still in decline.
The 1997 annual report of the American TPCC (Trade Promotion Co-ordinating Committee) showed a declining US share of the Asian export market. While the US had increased its share of exports to Mexico, Argentina and Brazil, the US's market share in China, India, and South Korea (as well as in South Africa and Turkey) had declined.

Financiaria, Viento Sur, 40, October,1998.

The share of total US exports that went to Asia increased from 15% in 1990 to 20% in 1996. But its share of total exports to the region in 25 key product categories fell from 13.5% in 1990 to 12.3% in 1996. Japan's share fell from 20.5% to 18% and the EU's from 16.4% to 15.7%. These declines can be explained for the most part by the rise of intra-Asian exports: their share rose from 34.2% in 1990 to 38.6% in 1996. "However, in key instances, US share loss was due specifically to gains by Japan and the EU."[109] Table 2, below, using a different definition of Asia and excluding intra-Asian trade, underlines how weak the US position was, relative to Japan.

Table 2: G7 Exports to Asia in 1996

Exporting Country	% of Asian export market
USA	**29**
Japan	**43**
Germany	**10**
UK	**6**
Italy	**5**
France	**4**
Canada	**2**

Notes: Asia includes South Korea, ASEAN, India, Pakistan, China and Hong Kong. Total exports in 1996= $350bn

Such statistics suggest that by early 1997 the US campaign towards the region was failing.

Or was it? There is one weapon in the locker of the US Treasury which we have not yet looked at: its ability to exploit the Dollar-Wall Street Regime as an instrument for currency and financial warfare. The use of the DWSR as such an instrument is easily explained. The region's political economies did not suffer from the usual kind of third world vulnerability: domestically politically weak states whose weakness was expressed as high budget deficits leading to high borrowings and debts on international financial markets. The region's state were not indebted in this way. Their vulnerability to the DWSR arose in the first place at the currency pole of the DWSR. They were mainly reliant of export-led growth. This made them vulnerable to strong movements in currencies. Since their currencies were mainly tied to the dollar and they exported significantly to Japan, a low dollar against the yen boosted exports, but a high dollar against a falling yen hit their exports. During the early 1990s, as part of what many see as a deliberate politically-inspired US campaign against Japan, the US Treasury supported a falling dollar against the yen. This put very great pressure on Japanese

[109] Financial Times, 29th october,1997,page 10.

industries and they responded both by shifting new investment into the rest of the region to benefit from the low dollar, and through many voices being raised for the construction of a yen zone tying the region together under Japanese leadership. This would have been a catastrophic blow to the interests of American capitalism.

But with the appointment of Larry Summers as Undersecretary at the US Treasury in 1995, Washington reversed its dollar-yen policy and allowed the dollar to rise ever higher against the yen. This started to exert great pressure on the exports of many of the region's economies. At the same time, large flows of hot money started pouring into the region from the United States. Those states in the region which had liberalised their capital accounts to allow such flows entry found their currencies being pushed still higher by this inflow of hot money, while simultaneously finding domestic inflationary pressures building up. In 1996 flows into Indonesia, Malaysia, the Philippines and Thailand increased by 43% to $17bn.[110] Private flows to Asian emerging markets in the 1990s are given in Table 1. The effects of the squeeze on exports was to cause difficulties in very important parts of their private sectors and they were tempted to borrow abroad from US and European as well as Japanese banks to tide themselves over the export squeeze.

Table 1:Private Financial flows to Asian Markets (Billions of US$)

	1990	1991	1992	1993	1994	1995	1996
Total net private capital inflow	21.4	37.7	22.4	59.5	75.1	98.9	106.8
Net foreign direct investment	9.5	15.2	17.2	35.2	44.6	50.7	58.0
Net portfolio investment	-0.9	2.8	9.6	23.8	18.5	20.1	20.1
Net other investment	12.9	19.7	-4.5	0.5	12.0	28.1	28.8
Net external borrowing from official creditors	5.6	10.7	10.2	8.2	5.9	5.0	6.7

(Source: International Monetary Fund: International Financial Statistics and World Economic Outlook databases)

In short the combined effects of the two poles of the DWSR were, by 1997, ensnaring the region's economies in a trap. US dollar policy was the first critical precondition for the crisis. The success of the US government and of US financial operators in persuading a number of governments in the region to open their financial sectors to inflows of hot money was the second precondition. The actual flows of hot money that then occurred in 1995-7 were responding to the effects of falling interest rates in the US financial system in the middle of the US boom: they were seeking higher short-term royalties in the still rapidly growing economies of the region. They were the third critical precondition. All that was needed by the spring of 1997 was for someone to pull the trigger. That job was one for a handful of US hedge funds.

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[110] UNCTAD:World Investment Report,1997 (UN New York and Geneva,1997)

Intention and Action in the Run-Up to the East Asian Financial Crisis

The question, of course, arises as to whether the Clinton administration was consciously using the DWSR as an instrument of economic statecraft against the East and South East Asian economies. What is certain is that the dollar-yen exchange rate is in the policy gift of the US Treasury and Federal Reserve. Summers was deliberately organising a strong dollar against the yen and was fully committed to it. What we do not know is why he wanted the dollar to rise against the yen. One explanation is that he wanted to help out Japanese business and in particular to help it export more to the United States. Is there anyone in the world who would believe that? Another explanation is that he wanted to prevent any moves towards the creation of a yen zone. But the Japanese government had never joined the movement for such a zone. We are thus left with a mystery over the source of Summers' policy, unless he was interested in squeezing Japan's dollar-linked hinterland economies in the region. Everything that we know about the Clinton administration's obsession with the challenge of the region also points in this direction.

The Clinton administration was also, in the mid-1990s concentrating its campaign to end controls on the capital account upon East and South East Asia. Enormous pressures and inducements were being exerted to this end. There was no sign of such a campaign directed at Chile. The focus was on Asia. And so too was the focus on liberalising the entry of foreign financial services. This was directed especially at Thailand, Indonesia and Korea. The US government did not, of course, organise the flows of hot portfolio funds into the region. But they were bound to occur: the dynamics of such outflows of funds, linked to the domestic US business cycle are well known. US Treasury Secretary Rubin is an old hand from Goldman Sachs and understands these dynamics perfectly. As Nixon had foreseen back in the 1970s, financial markets can be used as instruments of US external policy.

As to bank loans to East and South East Asia, the US government always claimed during the Cold War that while German and Japanese banks worked hand in glove with their governments' political strategies, the US government approach was always different.[111] Yet there was, in fact, a strong element of government direction to US banks in the 1970s in the US banks' recycling of petrodollars to countries of the South.

But, of course, we can have no proof of intentionality and of co-ordination with the private sector on the part of the Clinton administration. This absence of proof is common to much work in trying to analyse the actual practice of economic statecraft. We must use circumstantial evidence.

Thus, to take a famous example, it might appear with hindsight that Paul Volcker, head of the US Federal Reserve understood at the time that when he sharply raised US interest rates in 1979 he would plunge much of Latin America into a major financial and currency crisis. But did he think of that before he raised interest rates? And did he raise interest rates *in order to achieve that result*? He has insisted that the problem was not uppermost in his thinking and

[111] See J. Andrew Spindler:The Politics of International Credit. Private Finance and Foreign Policy in Germany and Japan. (The Brookings Institution, Washington DC, 1984)

that the Fed anyway lacked the resources at the time to make a prior study of the impact of the interest rate rise on the region. We cannot just take his word for it. But circumstantial evidence suggests that we can believe him: there were obvious other domestic reasons for raising interest rates at least to some extent in 1979; and if he had realised he would cause a gigantic crisis in Latin America he would also, surely have realised that he would bring the US banks to the brink of total collapse. Volcker would hardly have wanted that.

On the other hand, when analysts who may be assumed to have excellent access to US policy-makers claim that the Reagan team deliberately used a high dollar and high interest rates in 1981-3 with the aim of exerting pressure on 'Socialist France' we may well view that as a case of economic statecraft, using monetary policy.[112] The source is credible and the political importance of the goal is all too obvious: the failure of the French drive for growth between 1981 and 1983 was to be viewed in Western Europe as the final defeat of Keynesianism.[113] Here then we have a typical example of the US government using the dollar as a major weapon in a campaign for strategic political objectives. And the significance for the Reagan administration in defeating the French experiment cannot be doubted.

C. Randall Henning of the main Washington think-tank of the US international financial institutions,[114] claims that American governments have frequently used its control over the dollar price as a diplomatic weapon in its dealings with Western Europe. Pointing out that the US is less vulnerable to exchange rate shifts than Western Europe, Henning writes:"When clashing with European governments over macroeconomic policies or the balance of payments, American officials often took advantage of this asymmetry. In several instances, the threat of a precipitous exchange rate movement pressed European governments to reflate or dampen their economies in accordance with American preferences."[115]

The circumstantial evidence in the East and South East Asian case points overwhelmingly towards strategic design on the part of the US Treasury. But design for what exactly? To weaken these countries in macro-economic terms, certainly and to generate financial instability and currency vulnerability. But to set them up for hedge fund financial warfare?

The activities of the big US hedge funds in the East and South East Asian crisis may seem to

[112] This claim is made by I.M Destler and C.Randall Henning in "Dollar Politics: Exchange Rate Policymaking in the United States (Institute for International Economics, Washington DC,1989). This institute is the main think tank of Wall Street financial institutions

[113] Interestingly economic statecraft involving monetary policy, such as these examples tend to be ignored in the literature, including in Richard Baldwin's otherwise important book, "Economic Statecraft". But Susan Strange, without using the term statecraft, has illuminated a great deal in her writings on politics and international money.

[114] The Institute for International Economics.

[115] C.Randall Henning: "Europe's Monetary Union and the United States" Foreign Policy, No.102, Spring 1996.

most of us to have been a bolt from the blue. Until the LTCM crisis of September 1998 most people had probably never heard of hedge funds. But for the leaders of the US Treasury they were central part of their everyday furniture. They had been the central actors in all the major currency and financial crises of the 1990s, such as those of the Italian Lira and the Pound in 1992, that of the franc and the EU's Exchange Rate Mechanism in 1993, that of the Mexican Peso in 1994 and a host of others. And when we speak of hedge funds we are not speaking of the more than 1000 such organisations scattered across the United States: we are talking about a handful of funds of this name which operate on the international currency markets and which have more or less unlimited access to really gigantic loans from the very biggest of the American banks. Although they are opaque and very secret about their operations, they are at the very summit of the American financial structure. And their power makes instruments like Suuper 301 or anti-dumping instruments look like pea-shooters. We must look a bit closer at how they operate.

Hedge Fund Financial Warfare

The growth of hedge funds operating in foreign exchange markets and especially in foreign exchange derivatives is a direct outgrowth of the DWSR with its wild swings of the dollar against the Yen and Mark. Foreign exchange derivatives can be used for genuine hedging (i.e. insurance) against swift, large changes in the exchange rates of two currencies (foreign exchange risk). We will explain how this hedging can be used and then look at the kind of speculative operation used by hedge funds. You may be doing business that involves you committing yourself to making purchases over a long period of time in France and the price is denominated in French francs. At the moment stirling is, say, high against the franc at 10 francs to the pound. But something could happen within three months to make the pound fall massively against the Franc to 5 francs to the pound. Purchasing at that time will cost you double what it does today. But in the derivatives market you can pay a bank a fee to gain the option of buying francs for pounds at 9.50 francs to the pound. If the franc stays at 10 to the pound all you lose is your fee to the bank. You only had the right to buy francs at 9.50 to the pound, but you didn't have to buy at that price. But if the franc does fall to, say 6 francs to the pound in 3 months time, the option covers most of your losses because it allows you to get your francs not at 6 to the pound but at 9.50. So this so-called forward foreign exchange derivative market protects you to some extent.

The key for the hedge fund speculators being able to use these forward markets lies above all in the size of the funds that they can borrow relative to the size of the market. If the speculator's funds are big relative to the market, he can shift market prices with his own funds then get a multiplier effect as other smaller speculators strengthen that price shift by following it, and as the multiplier effect proceeds, he can withdraw from his position, taking profits.

Using the same example of the Franc-sterling exchange rate, the speculator starts in the same way, except that he takes out huge forward contracts to sell pounds for french francs at 9.50 to the pound in 1 month's time: say forward contracts totalling £10bn.[116] For these he

[116] The speculator's counter-party bank can cover its position by simultaneously taking out a forward contract to sell francs for pounds in a month's time.

must pay a fee to a bank. Then he waits until the month is nearly up. Then suddenly he starts borrowing pounds again in very large volumes and throws them against the exchange rate through selling them. So big is his first sale of pounds that the currency falls, say 3% against the franc. At this point other, smaller players see the pound going down and join the trend he has started, driving it down another 3%. Overnight be borrows another vast tranche of pounds and sells into francs again, and meanwhile the word is going around the market that none other than the master speculator is in action, so everyone joins the trend and the pound drops another 10%. And on the day when the forward contract falls due for him to sell pounds for francs at 9.50 the pound in the spot market is down at 5 francs. He takes up his forward contract and makes a huge profit. Meanwhile there is a sterling crisis etc. etc.

The official line of the Washington Consensus and of IMF Managing Director Camdessus and Stanley Fischer (Camdessus's deputy and the central operational designer in the IMF) is that the hedge fund speculators are of little significance except as triggers which essentially reveal trends already present in the so-called fundamentals of an economy. The argument is that no speculator can engineer structural shifts in prices on financial markets because there are so many players on these markets and these players act largely rationally, linking their buying and selling to their judgements about the underlying economy concerned. (Fischer has had to become somewhat more nuenced, acknowledging "swings in market sentiment [which]...may on occasion be excessive, and they may sometimes reflect contagion effects, which may themselves be excessive on occasion."[117]

This is a superficial view, that can be defended only on the basis of experience in large financial markets operating normally with high levels of liquidity in large advanced economies. But as Joseph Stiglitz, the chief economist at the World Bank and many others, have pointed out, this is far from being the case for smaller, much less secure financial markets in smaller economies. Nor is it true even in advanced markets in many circumstances: the sudden fall of the dollar against the yen, by a staggering 10% in less than a week in October 1998, was widely put down to the action of one or two very large funds unloading dollars for yen. They had this effect because the market was thin: when few people are willing to buy (or sell) falls (or rises) are likely to be magnified.

The Camdessus view is also not shared by leading speculators in forward foreign exchange markets, for whom the size of the financial war chest of the speculator relative to the scale of activity on the given foreign exchange market is decisive. Bill Lipschutz, former top currency speculator for Salomon Brothers, explains this vividly in the following interview with Jack Schwager:[118]

"How is large size an advantage?
You're kidding.
No, I'm serious.
If a big buyer comes in and pushes the market 4% that's an advantage.

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[117] Stanley Fischer: "Capital Account Liberalisation and the Role of the IMF", paper to seminar on Asia and the IMF, September 19th,1997.

[118] From Jack D. Schwager: The New Market Wizards. Conversations with America's Top Traders. (Harper Collins, New York,1992)

He still has to get out of that position. Unless he's right about the market, it doesn't seem like large size would be an advantage.
He doesn't have to get out of that position all at once. Foreign exchange is a very psychological market. You're assuming the market is going to move back to equilibrium very quickly -- more quickly than he can cover his position. That's not necessarily the case. If you move the market 4%, for example, you're probably going to change the market psychology for the next few days. [In other words, when others see a big swing created by a powerful hedge fund, they follow its lead for the next few days, also buying, enabling the hedge fund to sell to them and take its profits.PG]
So you're saying size is an advantage.
It's a huge advantage in foreign exchange.
How large an account were you trading at Salomon?
That question really has no direct meaning. For a company like Salomon there are no assets directly underlying the trading activity. Rather, over time, the traders and treasurer build up greater and greater amounts of credit facilities at the banks. The banks were eager to extend these credit lines because we were Salomon Brothers. This is an example of another way in which size was an advantage. By 1990, our department probably had $80billion in credit lines. However, no specific assets were segregated or pledged to the foreign exchange activities." In mentioning $80Bn, Lipschutz was referring to the end of the 1980s. By the mid-1990s, the leverage available to the top speculative operators could be ten times that figure.

And Lipschutz's last answer brings us to the huge financial strike power that these big hedge funds can mobilise from the big US banks. One of the most dramatic revelations from the LTCM affair was the way it revealed that this fund had more or less unlimited access to loans from the biggest of the American banks. Although the activities of funds like LTCM, Soros's Quantum Group and Robertson's Tiger Fund are very secretive they operator right at the very centre of the Wall Street networks. The IMF has suggested these funds can borrow 20 times their capital, Soros admitted to 50 times. But the LTCM was revealed to have borrowed 250 times its capital base.[119] The main hedge funds are supposed to have a combined capital base of $300bn dollars. Let us assume that their leverage is only 100 times their capital (and not the 250 times of LTCM). That would give them a collective leverage of $30 trillion. Of course, they don't all work together: only some of the top hedge funds do. Thus, attacks on currencies are usually the work of half a dozen of the biggest hedge funds operating together. They can mobilise funds far larger than the GDP of middle sized rich OECD economies like, say, Australia.

The derivatives markets dwarf all other financial sectors and the biggest of these derivatives markets is that for foreign exchange derivatives. A 1995 study by the Bank for International Settlements put the total principal in foreign exchange derivatives at $16 trillion.[120] While daily turnover in the ordinary foreign exchange market was $520billion in April 1995, daily turnover in the foreign exchange derivatives market in that month was $740billion.

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[119] IMF: part IV.Developments and Prospects in Emerging Markets, page 33.

[120] Bank for International Settlements: 'Central Bank Survey of Foreign Exchange and Derivatives Market Activity' May 1996.

It might be thought that such a huge market would involve a large and diverse collection of operators. Yet this is not so. The centres of this market are in the US, in London and in Canada and no less than 75% of business in these centres in handled, according to an IMF study, by just 10 hedge funds.[121] And these ten companies work very closely together. The great bulk of their business is 'over the counter' (OTC) rather than within exchange institutions and it is totally unregulated. And they are very secretive. According to the IMF, some 69% of foreign exchange derivative business is conducted between these dealers. And collectively these companies can mobilise enormous financial resources. The IMF estimates that the foreign exchange derivatives hedge funds can mobilise between $600billion and $1trillion to bet against currencies in speculative attacks.[122] This is truly staggering fire power.

There is no doubt whatever that the hedge funds were the driving force of the attack first on the Thai baht, then on other regional currencies and the Hong Kong stock market. The first hedge fund assault on the baht occurred in May 1997, one month after the Clinton administration launched its campaign demanding that Thailand and Indonesia open their financial sectors fully to US financial operators. Thailand was the most vulnerable target for attack because it was actually the most open economy in the region, the one whose government had adopted a model closest to US demands. It was also suffering from that typical feature of American-style open financial systems -- a large speculative bubble in its property market.

The central roles of the hedge funds in the triggering of the Asian crises of 1997 was fully reported at the time by the Financial Times and other financial papers.[123] Yet much of the mainstream Anglo-American media have treated this as if it was the paranoid populism of Malaysian Prime Minister Mahatir. Mahatir was simply stating a fact about the role of these operators. And he was not alone. A dispute amongst the IMF directors themselves has exploded into public view on this question, an unprecedented event. Under pressure from East and South East Asian governments, as well, perhaps, as fellow directors of the IMF, Managing Director Camdessus agreed to carry out an investigation of the hedge funds' activities in the crisis. He then chose mainstream American economists for the job. When the report came in, Camdessus agreed with it. But other IMF directors did not. They considered the report unsatisfactory because it underplayed the role of these institutions in the crisis. They did not just disagree. They insisted that Camdessus publicly record the disagreement in the main report of the Directors for the autumn 1998 Washington IMF conference. This is unprecedented in IMF history. It suggests much more than an analytical disagreement: a belief on the part of directors that they were faced with some sort of cover-up on the issue.

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[121] Coenraad Vrolijk: Derivative Effects on Monetary Transmission (Working Paper of the International Monetary Fund, WP/97/121, 1997)

[122] 'Mahathir, Soros and the Currency Markets' The Economist, 27th September,1997.

[123] See the Financial Times for the last week of May 1997 and the first two weeks of July 1997.

Of course one of the reasons for the extreme sensitivity of this issue is because the US government must have been very well informed about the activities of these hedge funds. They would know this because the Federal Reserve would know that the big US banks were bankrolling the East Asian operations of these funds. US intelligence would also be informed. The main banks of any state work extremely closely with their state.[124] Commonly governments get their leading private sector banks to extend credit to a foreign government or large company in the furtherance of foreign policy objectives. And the top banks can in turn gain access to intelligence information from their governments, important for assessing political and other kinds of risk. All this is so to speak normal. US officials always used to argue that the US government was different from others in this respect. Such claims may have carried some force during the Cold War. But after the damage done by the US hedge Funds to Clinton's Mexico policy in 1994-5, it is scarcely credible that the US government would have done nothing to bring some oversight, at the least, over what its hedge funds were up to. If US intelligence has, as we know, been largely switched towards economic and commercial intelligence we can doubt that this work is confined to the small change of negotiations on business deals while steering clear of the politically absolutely central field of international finance.

But whatever the exact relationship between the activity of these funds and the activity of the US Treasury, they were both acting in the same direction in the summer and autumn of 1997.

PART FIVE: THE POLITICS AND ECONOMICS OF THE PANIC OF 98

The Asian crisis began in Thailand at the start of July 1997. The next economy to fall was Indonesia. But the really decisive financial crisis was that of South Korea. It was the South Korean crisis which ended the temporary stabilisation of Indonesia and which finally brought complete collapse there. And the South Korean crisis was responsible for plunging the whole region into slump.

The general pattern of the crises is easily summarised. Hedge funds attacked currencies, eventually breaking the Thai Baht then the Indonesian Rupiah. These hedge fund attacks led the US mutual funds and the triad's banks as well as other financial operators to pull their funds out of the countries concerned. As the funds poured out, currencies collapsed further and there were two immediate effects: first, local banks could not continue to roll over their dollar debts through new borrowing because the Western institutions were no longer lending; and secondly, as currencies collapsed, the size of the dollar debt in terms of local currency resources leapt upwards. This double blow then fed through to the rest of the financial systems of the countries affected as local banks refused new credits to industrial companies, threatening them with insolvency. A vicious downwards spiral ensued threatening a complete collapse of the financial systems upon which any capitalist economy depends for economic activity.

[124] See, for example, J.Andrew Spindler:The Politics of International Credit.Private Finance and Foreign Policy in Germany and Japan. (The Brooking Institution,1984)

Until the summer of 1997 the East and South East Asian states had managed for a quarter of a century to avoid being entangled in the lethal, intersecting steel wires of what might be called the twin yo-yos of the Dollar-Wall Street Regime: the currency yo-yo of the dollar-yen-mark exchange rate, throwing trade and investment relations one way then the other; and the financial yo-yos of hot money and short-term loans whizzing into the financial nerve centres of regions' economies and then whipping back out again. No government in the region could do anything about the swings of the yen-dollar exchange rate: they could only try to adjust their exchange rate policy and domestic macro-economic conditions to try to cope. But those states which had succumbed to the pressures of the US government, the IMF and the Wall Street institutions to open their capital accounts and domestic financial sectors to some extent were allowing their economies and populations to enter a mortally dangerous trap: the inflows of the hot money and short-term loans arrived like mana from heaven, because they seemed to enable these states to evade the effects of currency fluctuations and thus to evade hard domestic adjustments through credits from the Anglo-American financial centres. But it was not mana: it was bait. When the financial sectors of the region bit into it they were hooked, trapped in the sights of the US hedge funds, sitting ducks for financial warfare. The hedge funds struck, the lines of credit were wrenched back into London and New York and economy after economy was dragged, writhing like a wounded animal onto the operating table of the IMF and the US Treasury.

Of course, not all the East Asian economies were dragged directly into the crisis. Those which had refused to bow to American pressure to dismantle their capital account controls escaped the onslaught because the hedge funds could not hit them. The factor that turned a state's failure of macro-economic adjustment into a catastrophe was the degree to which the Asian development model had been breached by liberalisation of the capital account. Those countries which had largely kept their capital controls were protected from the financial attacks which followed: China, Taiwan, Vietnam and India. Those that had liberalised in the key areas found their macro-economic management failures exploited by devastating speculative attacks. And even Hong Kong which could not have been said to have had serious macro-economic problems but did have a liberalised capital account was to be subjected to sustained, repeated hedge fund assaults for more than a year.

Despite this, as in the past crises in other parts of the South in the 1980s, Anglo-American leaders and propaganda media were quick to politically exploit the crisis, making the intellectually illiterate claim that failures to manage exchange rate volatilities and conjunctural financial sector instability proved the bankruptcy of the East Asian growth model and the universal validity of the Anglo-Saxon model of capitalism.[125]

As throughout the history of the DWSR, the East Asian crisis was to be a case of what might be called the team-work between the spontaneous drives of the financial forces of Wall Street and the political will and ingenuity of Washington. As the crisis spread across the region, the US Treasury and the Federal Reserve were serene about its global consequences.

[125] An exception to this truculent and illiterate triumphalism which partially saved the professional honour of Anglo-American journalism was to be found in the honesty and moral courage of Martin Wolf's writing in the Financial Times and in many, though not all of the Financial Times's editorials.

They knew from a wealth of past experience that financial blow-outs in countries of the South provided a welcome boost for the US financial markets and through them for the US domestic economy. Huge funds could be expected to flood into the US financial markets cheapening the costs of credit there, boosting the stock market and boosting domestic growth. And there would be a rich harvest of assets to be reaped in East Asia when these countries fell to their knees before the IMF.

But Rubin, Larry Summers and Alan Greenspan made four analytical errors. First they failed fully to grasp the fact that East and South East Asia was no longer just the South: it was a dynamic and weighty component of the world economy. A deep crisis there would transform the economic equations of those economies outside the triad which supplied inputs for the East and South East Asian boom. These commodity producers would see their export prices slump. This fact in itself need not have alarmed Rubin. On the contrary, the prospect may have delighted him. Declining relative prices of commodities from the South had been one of the keys to the non-inflationary American boom.

But if Rubin was taking this view of the likely fall in commodity prices, he was guilty of American-centred thinking and forgetting another context upon which the commodity producers' falling export prices would impact: the endemic structural financial fragility of these commodity producing countries as a result of the past triumphs of the DWSR. Countries like Russia and Brazil may have been turned successfully by the DWSR into a honey-pot for Wall Street financial operators but they were honey-pots precisely because they were so much weakened by debt burdens. A weakening of their and many other similar countries trade prospects as a result of the East Asian crisis could tip them over the abyss as financial operators saw the threat and fled.

And the third problem that Rubin did not fully grasp was that the huge growth of speculative forces within the US financial system itself could be sustainable only through constant expansion. Like the pyramid funds of Albania such speculative forces can sustain losses on betting with borrowed money on the part of some players only through the bulk of the others being able to throw more money onto the table and to make fresh gains. With multiple financial crises occurring simultaneously in many places, the speculative forces on Wall Street could find that the banks bankrolling them could lose confidence in continued expansion, fear collapse and then move to create it by refusing further lending.

Analytical failures of these kinds were to lead Robert Rubin to approach the Asian crisis not just with serenity but with excitement and enthusiasm. As we shall see, the US Treasury was to view the crisis as an historic opportunity which, if seized, country transform the future of American capitalism, anchoring its dominance into the 21st century. This was the fourth problem that Rubin failed to foresee: the problem of Rubin himself as an actor in the crisis.

We will not review the details of the course of the East Asian crisis.[126] We will focus only

[126] Those who wish to do so should read the articles by Wade and Veneroso, the second article by Wade and the article by Cummings in New Left Review. They should also read the article by Walden Bello op. cit and other material in that issue of the Review of International Political Economy. A very full chronology of the crisis and a large and very useful archive of other material on the crisis can be found at N. Roubini's web site at New

on the responses of the Japanese and American governments to the crisis and in particular on the stance of the US Treasury towards the decisive moment of the East Asian events: the South Korean financial breakdown. We will then look at the structural reasons for the transformation of the Asian crisis into a generalised international financial panic in 1998. And we will conclude by considering whether they may be a pathway of the 'globalization'.

Tokyo's Crippling Defeat

York University Stern.

As the Asian crisis spread across the region from Thailand in July and August 1997, the most affected states turned to other states for help. The US government refused to take any positive action to stabilise financial systems and currencies and kept the IMF on a leash. At the height of the Thai crisis in August, the US government's response was to send a delegation to Bangkok demanding further liberalisation of Thai markets to improve access for American capital.[127] Japan therefore faced a decisive test, the biggest political test it had faced for, perhaps, 50 years. It could take upon itself the task of leading the region out of crisis, but in doing so it would challenge the political authority of the IMF and the central strategic drive of the US. But if the Japanese government remained supine and let the Clinton administration dictate events and terms, the consequences for Japanese capitalism could be extremely grave. Its financial system, already in serious difficulties, could be dragged down by its very heavy exposure to the region and the US would be likely to exploit this weakness up to the hilt.

The Japanese government attempted to steel its will to intervene politically. It came forward with a proposal that it would manage an Asian consortium, an Asian Monetary Fund (AMF) to stabilise affected countries. This initiative drew strong support from governments in the region. Particularly striking was the Chinese government's support for the plan, an unmistakable sign that a regional coalition between Japan and China was a distinct possibility. The Thai rescue package was the result of the work of the Japanese government in putting together a coalition . But at the last moment the IMF and the US entered the scene to put their trade marks on it to prevent an open Japanese challenge to IMF global control. But still the Japanese government advanced its AMF proposal, suggesting that the fund could have $100bn of financial resources.As one analyst explained "[US] Treasury officials accordingly saw the AMF as more than just a bad idea: they interpreted it as a threat to America's influence in Asia. Not surprisingly, Washington made considerable efforts to kill Tokyo's proposal."[128] In this, the Clinton administration was able to enlist the support of the West European governments, who joined the campaign to exert the maximum influence on East and South East Asian governments to turn away from the Japanese proposal. In an interview with Larry Summers of the US Treasury, Institutional Investor explains: "Concerned that Japan was proposing the idea [of the AMF] as

> A step toward hegemony in the region, but unwilling to bring such a sensitive issue into the open, US and European financial officials worked the phones with South East Asian officials, talking down the idea and hoping it would die quietly..."[129]

The later Indonesian IMF deal did include a substantial American and West European

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[127] Michael Vatikiotis: "Pacific Divide", Far Eastern Economic Review, 6th November,1997.

[128] Reic Altbach: "The Asian Monetary Fund proposal: a case study of Japanese regional Leadership", Japan Economic Institute Report, No.47A, 1997.

[129] Institutional Investor, December 1997, quoted in Ron Bevacqua: "Whither the Japanese model? The Asian economic crisis and the continuation of Cold War politics in the Pacific Rim." Review of International Political Economy, 5,3, Autumn,1998.

involvement, as a means of combating the Japanese threat. By November of 1997, the will of the Japanese government to offer the region a path out of the crisis which would evade the strategic goals of the US government was broken.

The full story of the dramatic diplomacy surrounding the failed Japanese demarche has yet to be told.[130] But Japan suffered a stunning political defeat inflicted by the US with the support of the EU. The basis for EU support for the US Treasury throughout the crisis is also a story whose details remain obscure, but one with great significance for the future.

American Government Tactics over Korea

The IMF's Indonesian package did, for a while, seem to work. In the first week of November 1997, Michel Camdessus felt confident enough to declare that the IMF had succeeded in breaking the vicious circles of financial collapse in the region.

But just at that moment, the financial problems in South Korea became critical and the Japanese financial system was simultaneously gripped by panic. This was the first really critical point in the transition from a purely East Asian financial crisis to a world financial panic. South Korea's economy is larger than those of Thailand, Indonesia and Malaysia put together. The evolution of the Korean crisis in November and December 1997 produced the shipwreck of both the Indonesian and Thai economies and triggered the transmission of the crisis to the financial centres of the West as well as Russia and Latin America.

But the central characters in the Korean drama of late 1997 were not simply or mainly international and Korean bankers. The denouement was produced by Robert Rubin and Larry Summers in the US Treasury Department. They have made no attempt to conceal the fact that they ran the IMF operation on Korea.[131] They decided that the IMF should be used not in the ways it had operated in the last 50 years but instead in the new ways in which it should operate in the 21st century. For the US government, Korea was going to be a first.

It is the behaviour of the American government in the terms it required the IMF to impose upon South Korea that has caused the most controversy amongst those who had formed part of what has been called the 'Washington Consensus'.

The reason for the debate about the US government's role lies in the fact that its policy for dealing with the South Korean crisis was not only not geared to stabilising the won and the Korean banking system: it was not even geared to stabilising international financial markets. Instead it made its governing objective a drive to transform the internal social relations of

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[130] But see Bruce Cumings: The Korean Crisis and the End of 'Late' Development", New Left Review 231,1998. See also Walden Bello, op.cit.

[131] Interviewed on the US TV programme News Hour, Rubin was asked by Jim Lehrer why he had been working so hard on the Korean IMF programme. Rubin replied:"Jim, American leadership has been absolutely central to this effort...in today's world the United States is really the only country that is in a position to provide the kind of leadership that is needed to deal with issues of this magnitude and importance to our country." Newshour, 13th January,1998 (http://www.pbs.org/newshour)

production within South Korea and to risk the *deepening* of the Korean crisis and the *continuation* of international financial panic in order to achieve that transformation.

In financial crises like that in Korea, the traditional task of the IMF is simultaneously to stabilise the exchange rate and to find a way of reassuring international financial markets about the solvency of the South Korean banks. This dual operation will then provide time during which domestic economic activity can continue thus providing a context in which a restructuring of the banking system can take place.

Yet in the case of South Korea, the IMF programme was not designed to restore investor confidence *in Korea* at all, nor was it designed to revive activity on the part of Korea's main economic operators. It was instead a domestic transformation programme that would inevitably undermine investor confidence in the institutions of Korean capitalism.

The siege of the South Korean currency, the Won, began on 6th November, the day when IMF Managing Director Camdessus was explaining that the IMF package for Indonesia should break the vicious cycle of economic destabilisation in Asia. Between 6th November and 17th November the Korean government sought to defend the Won, before abandoning the struggle on the latter date and closing the foreign currency market for three days. On 20th November the government asked the Japanese government to persuade Japanese banks to roll over their short-term loans to Korea. But the East Asian crisis was now plunging Japanese financial institutions, deeply engaged in the region, into crisis: one of Japan's four biggest securities houses, Yamaichi, would collapse 4 days later. So the Japanese government was paralysed. The following day, the 21st November, the South Korean government announced that it was asking the IMF for a rescue package.

Negotiations with the IMF then dragged on for a full two weeks. On Monday 1st December the IMF and Korea had still not agreed a deal: they were disagreeing about the growth target for the following year and about the IMF's demand that 12 merchant banks should be closed. The following day US Federal Reserve Chairman Alan Greenspan said that the Asian crisis was likely to accelerate the move from large amounts of government-directed investment to a system that encourages more private sector involvement: this was a clear statement that the US authorities required a radical break with Korea's model of capitalism. Finally, on 4th December, agreement between South Korea and the IMF, totalling $57Bn was announced.

Senior officials in the US Treasury Department were well aware that the IMF's Korean programme was something different from the usual IMF operations: something new. As reported by the Financial Times the programme was " a strategy carefully crafted by the US and the IMF that was intended to provide the blueprint for what US officials have confidently claimed as a 'genuinely 21st century response to the first 21st century financial crisis'......"[132] The details of the strategy were worked out by Treasury Under Secretary Larry Summers in Manila and US Treasury officials managed the extremely difficult negotiations with the Korean government from a suite within the same hotel in Seoul as the IMF delegation. It seems that the IMF officials within the region were ready to settle on the basis of more lenient terms with the Korean government, but they were prevented from doing so by US Treasury officials who had the backing of IMF Managing Director, Michel Camdessus.

[132] Financial Times, 2nd January,1998, page 3.

The US's 21st Century Solution: Transforming The Social Relations of Korean Capitalism

The IMF programme for Korea had 2 main parts:

1. Protecting the interests of creditors and the stability of the international financial system.
2. Korean Economic Management and Social Transformation.

1. Protecting Creditors and the Stability of the International Financial System.

The central element in this part of the package was, of course, the provision of funds from G7 states and multilateral organisations to Western financial institutions which were exposed to the Korean debt crunch. Formally these funds were, of course, advanced to the Korean government, but only in order for them to flow straight back into the hands of Korea's private creditors. Thus, the Western lenders which had flooded the Korean market with loans and then suddenly withdrawn were to be rewarded with what the Financial Times's leading commentator called 'vast bailouts of IMF money'. [133]

Yet sums advanced by the G7 and multilateral organisations did not cover the full amounts of Korea's short-term debt obligations and much of the IMF package -- for example, the money committed by the US Treasury, was not supposed to be used for such pay-backs: it was last resort, standby money. Thus, the package envisaged that the Korean government would take immediate measures to generate domestic sources of pay-back funds. This new funding was to be generated by the Korean government sharply raising domestic interest rates and simultaneously sharply tightening domestic fiscal policy to strengthen its own financial position. It had to commit itself to massively increasing domestic interest rates while simultaneously tightening its fiscal policy. Short-term interest rates had to be raised to over 21% -- a real rate of 15% and there was to be a tightening of fiscal policy by a huge 1.5% of GDP. Against this background, the American banks were preparing to come forward with a new loan to the Korean government at penal rates of interest but of sufficient size to cover the short-fall in the international support package.

[133] Martin Wolf:'Same old IMF medicine' Financial Times, 9th December,1997,page 18

Thus the protection of Western creditors was to be achieved through the transformation of the Korean financial crisis into what would be likely to be a complete domestic financial breakdown within Korea itself. When domestic financial crises occur, the economic task of governments is to pump more money into the banking system and to lower interest rates in order to restore the creditworthiness of the banking system and in order to restimulate the industrial sector so that it too can maintain its creditworthiness. But the IMF package involved bailing out international creditors by making a bad Korean domestic crisis catastrophic. In the words of Martin Wolf of the Financial Times, the IMF demanded a 'damagingly tough squeeze on economic activity....If the illness is debt deflation, a significant economic slowdown must make the patient's condition worse.' The IMF package was 'little more scientific than for a doctor to bleed his patients.'[134]

The IMF package indeed included further requirements that would intensify the domestic collapse: thus, despite a devaluation against the dollar of 30%, which would automatically push up domestic prices substantially, inflation was to be kept at 5%. In yet a further squeeze, the Korean banks were required to switch rapidly to international standards , so they had to build their capital base and make bad loan provisions instead of offering credit to the industrial sector. The result was to be a severe credit squeeze.[135] Martin Wolf summed up this aspect of the IMF programme as follows:'The conclusion: however sick Korean companies and banks may be now, they will soon be sicker.' This prediction proved accurate. A Financial Times editorial in May 1998 noted that "the pain [of the East Asian crisis] is proving worse than many anticipated. The need to combat recession looks like becoming as urgent as the previous priority of restoring market confidence. There is no point in endorsing a cure that ends up killing the patient."[136]

2. Social Transformation and foreign capital access measures.

The slump-generating elements in the IMF package should not be seen only as an internationally costless way squeezing debt repayments out of Korea. They were evidently designed to create the necessary domestic framework of economic incentives for completely reorganising the institutions of Korean capitalism, destroying what Robert Wade has called Korea's Asian Development Model. A Financial Times editorial explained the general goal of the package: 'For Korea this must mark the end of an era of dirigisme that contributed to its extraordinarily successful development. But this crisis has shown that such interventionism cannot be combined with freedom to borrow abroad. Since the latter can hardly be halted, Korea has no choice: it must liberalise systematically.'[137]

Under the IMF package, the chaebols would be turned into Western-style companies, placing short-term profits first, relying upon share issues and largely depending upon internal savings

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[134] Martin Wolf:'Same old IMF medicine' Financial Times, 9th December,1997,page 18

[135] Quoted in Financial Times, page 19, 11th May , 1998

[136] 'Agony sets in for Asia' Financial Times, page 19, 7th May , 1998

[137] Korea's Rescue, Financial Times, 4th December 1997, page 25.

for their new investments. Thus, as the Financial Times commented: ‘A reduction in Bank lending will force [the Chaebol] to turn to capital markets, subjecting them to investor discipline as corporate transparency improves and family owners yield control. This process will come with a high cost.....”[138]

The squeeze was carefully crafted to hit the chaebols very hard. Thus, it included a specific ban on public works programmes, something which the Korean government has traditionally used to help the Chaebols, many of which have been engaged in government-funded public works construction.

[138] Financial Times, 4th December, 1997, page 6.

The drive against the Korean Development Model was combined with requirements for sweeping Open Door measures allowing the fullest possible access for foreign capital. major feature of the IMF programme was the insistence on faster and fuller opening of Korea's doors to entry and exist by foreign capital both in the banking and corporate sectors. Specifically, foreign investment in domestic financial institutions and domestic equity were to be liberalised; domestic money and bond markets were to be opened to foreign investors, and restrictions on foreign borrowing by domestic corporations are to be lifted.[139] The ceiling on foreign ownership of shares in Korean companies was to be raised from 26% to 50% as from 15th December. Japanese products were also to be given bigger access to Korean markets. (Previously Japanese exports to Korea had been limited because of Japan's large trade surplus with Korea. Under the agreement \$5.5bn was to be delivered to Korea the following day and a further \$3.6bn would be disbursed on 18th December assuming that the first review of Korea's programme of internal changes was satisfactory.

The Failure of the US Government's Drive for a 21st Century Solution

The relief in international financial markets when agreement was finally announced between the IMF and the South Korean government lasted less than twenty four hours. When international operators actually read the agreement, they fled from Korea in panic, so that the following day the country was plunged into a downward spin. But this did not surprise or alarm the US Treasury. Indeed, they indicated when the package was announced that they were not expecting any quick restoration of confidence. For the next two weeks, as the Korean crisis deepened as a result of the IMF programme, Treasury officials remained unbending and confident about the package.

On the 5th December, the day after the IMF agreement, the Won started plunging again so that by 8th December it had fallen about 16% since 3rd December. The reason for the fall was very simple arithmetic: IMF package did not cover Korea's short-term debt servicing and a new wave of contagion spread across the entire region. On 10th December an IMF document was published showing that the Korean deal involved closing some of Korea's big commercial banks and this created new waves of panic. On 11th December there were huge losses in stock markets across the region[140] and the panic spread to Wall Street and to Latin America. On 12th December the Korean won fell to 1891.40 to the dollar whereas to had been 1,170 to the dollar at the time of the IMF package 9 days earlier. In short, the IMF stabilisation package was no such thing: it further destabilised the Korean economy.

[139] Martin Wolf:'Same old IMF medicine' Financial Times, 9th December,1997,page 18

[140]: HK down 5.5%, Malaysia 7.4, Indonesia 4.6, Singapore 2.3, Philippines 4.9, Thailand 4.9. and there was a new wave of pressure against the Hong Kong dollar.

Yet the US government calmly indicated that it was not prepared to change its stance. Treasury Secretary Rubin stated that implementing the IMF programme was “the absolute key to....re-establishing confidence in the financial market.” This again was a new concept: in the past, *the announcement of agreement* on a rescue package was supposed to stabilise an economy in payments difficulties: implementation came later. But Rubin was saying that confidence and thus stability would be restored in Korea only after a first wave of implementation of the transformation programme. Rubin’s Treasury officials and those of the IMF said South Korea must carry out the reforms before there could be any talk of new money. The IMF would release a further $5.6bn by January 8th only if Korea stuck to its schedule of promised domestic changes.[141]

But on Friday 12th December, the Indonesian crisis acquired catastrophic proportions as the Rupiah fell 11% in a single day and lost 22% during the week (54% during the year).[142] At the same time, signals from Seoul suggested that South Korea was going to break with the IMF deal and simply default on its private sector’s debts. And this threat of a Korean default in turn raised fears in Wall Street and London of a systemic crisis in the international financial system.

It was only at this point that the US Treasury finally itself panicked and drew back from its ‘21st century solution’. On Monday 15th December the US Treasury back-tracked and the IMF said that its executive board meeting would consider that day the speedy delivery of further money to South Korea. The IMF said it was responding to a request from the Korean government, but Korean government officials said they were unaware of any such request having been made.[143] The ‘request’ in other words, seems to have come from Wall Street. The following day the won soared up 16% against the dollar, the stock market rose by nearly 5% and equity markets across the region also revived. On 16th December, the US Federal Reserve Open Market Committee shifted its own policy guidelines by failing to raise interest rates as US domestic indicators would have required. And on 17th December, the Japanese government gave a stimulus to the Japanese economy with a $15.7bn tax cut. The dollar fell sharply lower against the Yen, while stock markets across the Asian region shot up. And on 18th December the IMF disbursed the second tranche of $3.5Bn out of its loan package, despite the failure of South Korea to fully comply with the schedule of reforms in the original package.

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[141] N.Roubini, op. Cit., page 31. This involved lifted restrictions on foreign investment and making its banking system ‘more accountable to market forces’. Another key IMF condition was the for Korean government to curtail public spending -- in other words public works projects, the lifeblood of the construction companies around which many of Korea’s Chaebols are built.

[142] The subsequent collapse of the Indonesian financial system, followed by the collapse of the Sukharto regime should be seen as an unintended by-product of US policy towards Korea at this time.

[143] N.Roubini, op. Cit., page 33.

Yet the crisis was still not over. On Monday 22nd December after Moody's rating agency downgraded the foreign currency ceiling for Korean bonds and currency, the won fell from Friday's 1,550 to the dollar to 1,715. The Tokyo and New York stock markets fell. On 23rd December the World Bank disbursed a $3bn loan to South Korea -- its share of the IMF-led rescue package. By the 24th December, US financial markets were gripped by the fear that South Korea would still have to declare a debt moratorium. The Wall Street Journal reported that the US government's part of the IMF-led package -- $5bn, which was supposed to be a back-up sum to be used only as a last resort -- might now be thrown into the breach; it also reported that US banks were discussing restructuring their loans to the South Korean private sector, providing debt relief. Later that day, the IMF, the US and 12 other governments pledged to send an new tranche of $10bn but said that for a South Korean recovery it was critical that international commercial banks agree a 'significant' rescheduling for Korean financial institutions. The IMF said it would be disbursing a further $2bn (from its $21bn total) to South Korea on 30th December and a further $2bn on 8th January. The US and 12 other OECD countries said they would be sending $8bn (out of their pledged $24bn) by early January -- this was money pledged to be used only as a last resort. Of this total,$1.7bn would come from the US, $3.33bn from Japan.[144] US Treasury Secretary Robert Rubin said: "This is a major world event...It seemed appropriate for the [G7] industrial countries and other nations involved in the second line of defence to move their aid effort forward.". The 'major world event' he was referring to was not a Korean one but a threatened breakdown in American financial markets, unable to stand the strain of the US Treasury's political demarche on Korea.

The US Treasury's climb-down was, in fact, a stunning defeat. As the Financial Times reported, US Treasury officials " know that the critical decision to add an extra $10bn from the IMF, US, Japanese and other government resources and to engage the banks in a debt rescheduling exercise is a stunning policy reversal that could have big implications for the way future financial crises are tackled..... 'The fact is, the official sector looked a default by Korea in the face, and blinked,' said Morris Goldstein, a senior economist with the Institute for International Economics."[145] The US Treasury itself claimed that its climb-down was no such thing because the extra money and the involvement of the US private banks in rescheduling Korean loans was combined with further conditionalities being imposed on Korea for faster and deeper restructuring of its capitalist system. But nobody else saw matters in that way.

The backtracking by the US government did prevent the Korean default. But it did not end the wider financial panic: Indonesia was left with a complete credit crunch and effectively a complete default on its debts. The whole region was galloping into a deep depression which in turn would spread the effects of the Asian crisis to other parts of the world, particularly commodity producing countries Like Russia which would find world demand for their exports slumping and would thus face an exchange rate and financial crisis of their own.

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[144] Robert Rubin explained that the US contribution would come from a special fund administered by the US Treasury that did not require Congressional approval.

[145] Financial Times, 2nd January,1998, page 3.

But the important point about this central episode is the fact that the US government *sought to use panic in the private markets dealing with Korean currency and debt as a political lever* to further its policy objectives within Korea. And it was the American financial market's leading operators which exerted pressure upon the US government to stabilise the Korean economy. It was, of course, embarrassing for the US Treasury to be sitting down with private bankers to agree the rescheduling of private loans to Korea. But for the US and other Western banking communities, rescheduling the Korean debt with the US Treasury was a welcome relief.

As the shocks from financial crisis worked their ways through the Asian economies, the IMF's predictions about the region's growth prospects for 1998 turned out to be wildly out of line with realities. Deep slumps gripped much of the area with the most appalling suffering being experienced in Indonesia. But the hopes of the US government that it could reap substantial benefits for its capitals in the region as a result of the crisis did seem to be coming true. The battle for the future character of Korea's relations of production as a whole has continued to rage and it is by no means clear yet what the final outcome of that struggle will be.

But already in December 1997, American capital was looking forward to making a killing in Korea. The New York Times of 27th December reported that "Korean companies are looking ripe to foregin buyers". The Los Angeles Times of 25th January 1998 reported "US Companies See Fire Sale in South Korea". The Chicago Tribune reported on January 18th that "Some US Companies Jump into Asia with Both Feet". And the Wall Street Journal reported Coca Cola's purchases of companies in Korea and Thailand under the headline, "While some Count Their Losses in Asia, Coca-Cola's chairman sees Opportunities (February 6th). The gains in terms of US companies being able to take control over Asian assets have been substantial. As Hiromu Nonaka, secretary-general of Japan's ruling Liberal Democratic Party put it, in the summer of 1998: 'There is an invasion of foreign capital, especially US capital, under way. A type of colonisation of Asia has started.'[146] During the first 5 months of 1998, US companies had bought up double the number of Asian businesses that they had bought in any previous year, spending $8bn in total. Significantly the main target was the Japanese financial system, followed by South Korea and Thailand. The South Korean purchases have also been targeted especially on banking and finance. Securities Data, a US-based monitoring agency described the surge in asset purchases as an 'historic moment'. European companies, especially those of the UK, Germany and Holland have also been very active, spending about $4bn. This centralisation of Asian capital in Atlantic hands was intensifying as months passed. According to Goldman Sachs, the pace was 'certainly picking up'.[147] As Paul Krugman pointed out, the fact that the US purchases of business have been spread across many sectors including those where the US companies could not be thought to have a competitive advantage shows that the fire-sales are the product of weaknesses produced by the financial crisis.[148]

[146] Quoted in the Financial Times, 2nd June,1998, page 16

[147] Tony Walker: "US buys $8bn of Asian Business.", Financial Times, 15th June, 1998.

[148] See Paul Krugman: Fire-Sale FDI (http://www.nyuniversity.stern/nroubini)

From Asia to the Wider World

It is worth underlining the point that the big US investment banks were far from happy with the drive by Rubin and Summers (supported by Alan Greenspan at the Federal Reserve). Wall Street's dislike of Rubin's aggressive line had a simple explanation: his behaviour had created panic at the very heart of the international financial system, was dragging the Indonesian political economy into oblivion and was bringing some important speculators at the heart of the system close to collapse. The link between the DWSR and Asia would turn out to be a two-way street. While the centre of the international financial system stabilised in early 1998, this was only a temporary release. For the weight of the East Asian growth centre in the world economy would ensure that there would be an indirect boomerang effect on Wall Street via the effects of the Asian financial crisis on the product markets of the world.

This was the linkage that the US Treasury and Federal Reserve failed to foresee. As so often in the past the initial effects of the Asian crisis were beneficial for the US economy where things mattered most: in the bond and stock markets. Flight finance from Asia poured into New York, lowering bond yields and thus making speculation in shares on the stock market more attractive than ever.

But in the early months of 1998 it did indeed become clear that East and South East Asia were indeed heading for a deep economic depression. And because the region was the dynamic centre of the international productive economy, its depression quickly affected those economies producing the key commodity inputs for the world economy such as oil. The collapse in oil and other commodity prices was swift and it was soon reflected in oil producing states as great difficulties for oil producers like Venezuela and Canada and, of course Russia. Between September 1997 and September 1998 the price of oil dropped 33%, that of wheat fell 39%, that of copper fell 22%. The main indicator of commodity futures prices, the CRB-Bridge Futures Index, which covers 17 commodities, fell 18% between September 1997 and September 1998. The overwhelmingly proportion of the exports of so-called emerging markets are commodity based and since most of these emerging markets were heavily indebted and thus their financial systems and currencies were vulnerable to sharp deteriorations in their current accounts, the crisis spread.[149]

The Russian collapse was the next decisive phase of the crisis. The Russian crisis was the next big test for the US Treasury. Yet again it put together an IMF package and yet again this was inadequate and in August 1998 the rouble collapsed. The US Treasury could have stepped in at the last minute with some sort of emergency rescue. If it had been able to understand the real situation it was in it would certainly have done so. But Rubin again failed to grasp the reality. Now he looked at Russia through a speculator's eyes. Russia's assets had been a bonanza for 6 years but the economy has been a steadily worsening disaster, shrinking without limits and tiny now tiny and largely irrelevant in the world economy. Why, he must have reasoned, bother about the ruble collapse?

But he overlooked two facts. First, the Russian elites were not rooted capitalists at all. And

[149] See Michael M. Phillips: "Plunging Commodity Prices Spread Turmoil in the Global Economy", the Wall Street Journal, 27th August,1998.

secondly, a quarter of a century of the Dollar Wall Street regime had left much of the rest of the world with fragile and vulnerable financial systems. In just about every financial crisis since the start of the 1980s, the governments which were hit felt that they could not risk repudiating their debts for one very fundamental reason: their financial systems were only the nerve centres of whole capitalist economies with multiple links with the international economy. To have simply repudiated debt would have jeopardised interests across much of their economies by threatening a period of isolation. Russia was different. Economic life in the country had been in tragic and uninterrupted decline throughout the 1990s. Russia did have a thoroughly 'modern' set of internationalised financial markets, but their prices bore no relation to actual activity in the economy. They were purely speculative markets in ownership titles and the Russian banks were the same: useful for sucking resources in financial form out of the Russian economy into the Anglo-American financial centre and otherwise engaged in pure speculation. The only significant link between Russia and world product markets was energy and strategic raw materials.

Thus, when the July IMF plan for Russia failed and new Western money was not forthcoming, the ruble was ready to plummet. This time Soros did not even need to enter the forward market in the ruble. He simply had to open his mouth and say that the ruble would collapse and it did. But what had not been expected was the response of the Russian government. It simply repudiated its debts on the bonds it had issued to international speculators. It did not seek negotiations, it did not beg for more help. It simply stated that although Western investors thought they had short-term government bonds at a certain rate of interest, they were wrong: they now had long-dated bonds at a much lower rate of interest. And although Western investors thought that they had hedged their currency risk (of the ruble collapsing) attached to their bond holdings by buying derivatives from Russian banks, they were wrong again. The money would not be forthcoming.

Since the Yeltsin government represented a very narrow layer of speculators whose money was safe in the Anglo-American financial centre, this was the rational course of action for the government. So narrow was the fiscal base of the Russian state -- in other words, so weak were its roots in the real life of the Russian economy -- that to hand over its meagre tax resources to Western bond holders would have been suicidal anyway. And the production links between Russia and the world economy were tiny anyway.

The Russian Default and the Fragility of Economies Weakened by Two decades of the DWSR

The Russian default was an enormous international shock because around the world there were so many economies whose public sectors and banking systems were full of international debt, built up over two decades of monetary and financial volatility and crisis. And this debt was now no longer locked into medium-term bank loans as in the old Latin American crisis of the early 1980s. It now took the form of securities -- bonds and stocks -- that fitted neatly with the interests of US rentiers and mutual funds, enabling them to escape markets instantly by selling.

The question they faced after the Russian default was: should they sell now? There might be no contagion from Russia to Brazil, with its large public debt funded by short-term bonds. But what if there was a failure in Brazil? This would drag down the whole of Latin America and spread wider. Therefore, these speculative investors had every incentive to behave prudently and withdraw their funds. And by doing so they would, of course, provoke the crisis that they were guarding against. These kinds of thoughts were suddenly transforming the patterns of security prices all over the world and this sudden shift was what seems to have brought a central US financial institution, the so-called Long Term Capital Management (LTCM) hedge fund to its knees. It had been betting on what it had assumed to be a one-horse race: that as monetary union approached in January 1999, the Italian bond market would converge with the German. But the Russian default suddenly moved the Italian bond market the other way despite the approaching start of the Euro.

But the LTCM was an accident waiting to happen. And the pressure on Latin American financial systems was also an accident prepared by the steady strengthening of ties across the world's financial markets in the form of hot money. The ties of hot money were themselves a reflection of the basic fact that so much of the world economy had become too fragile and risky for the long-term commitment of funds by the rentiers of the core economies. There was also a power relationship at work, of course. Governments desperate to roll over their debts would take whatever they were offered by Wall Street: if they were offered hot money, so be it. But this power relationship was itself an expression of fundamental economic weakness and vulnerability outside the core. Wall Street would not have been so powerful, if these economies had not been so dependent. So we are driven back to the origins of this dependency and they lie in the fact that the growth paths of much of the world's economies in the 1960s and early 1970s had been broken by the rise of the DWSR, plunging economies into crises which left them with chronic weaknesses and vulnerabilities.

And the same regime had fed back to the American economy itself. It had been able to 'benefit' from the DWSR by opening up Latin America and strengthening its exports to the region. By 1998 about half of US exports were going to Latin America and Asia. This had been a handy escape route for the American productive sector faced with the competitive challenge of Japan and Western Europe. The DWSR had offered a way out from the hard, domestic task of raising productivity levels and reorganising the linkages between savings and productive investment in the US economy. And the DWSR had another 'beneficial' effect as well: it offered paths to link the ordinary American to a speculative-rentier system whose power stretched ever deeper into the economies of the world. This was revealed with stark clarity by the Mexican crisis of 1994-5 as Time magazine explained at the time:

"What many Americans discovered last week was that for all the beltway rhetoric pitting Wall Street against Main Street, Wall Street long ago intersected with Main Street. At Risk in [Mexico] were not only US banks and giant investment firms but mutual funds held by tens of millions of little-guy investors who bet their savings on double-digit yields in emerging markets like Mexico. 'This wasn't about bailing out Wall Street' a congressional staff member said [of the rescue package], 'but about mutual and pension funds and that means average Americans.' "[150]

Time magazine was right about the facts, but the growth of powerful speculative forces within almost every sector of the US economy was greatly stimulated by the evolution of the

[150] Cited by Adam Harmes:"Institutional Investors and the Reproduction of Neoliberalism", Review of International Political Economy, 5,1, Spring 1998

DWSR. And by 1998 the US economy was inflated by very large and socially all pervasive speculative distortions: the stock exchange, despite the falls in 1998, remains the central inflated bubble.

The American bull market has continued, with a couple of notable interruptions, for 15 years and has become absolutely central to American capitalism. In the last 15 years equity prices have risen tenfold.[151] In the last three years the stock market has created more paper wealth -- in the sense of inflated asset prices, than in the previous three decades.[152] During this three year period, the cumulative gain on the Standard and Poor's 500 index has been 111%.[153] This amounts to $3trillion. By the spring of 1997, the value of US stocks finally exceeded the US's annual economic output of about $8trillion.[154] As Paul Krugman put it, these leaps in share prices could be justified only "if the US economy is poised to begin decades of extraordinary growth".[155] The bubble has been rising in the housing market in many parts of the USA as well and by October 1998 there was evidence that it was about to burst.

The entire US economy is now locked into the bubble. As the director of US Economics Research at Goldman Sachs put it: "The importance of the stock market in keeping this virtuous circle [in the US economy] intact cannot be overstated."[156] The banking systems on Main Street
and Wall Street as well as the mutual funds and pension funds are all hitched to the bubble. And so too is an extraordinarily wide constituency of ordinary Americans. Personal household debt ratios in the USA have never been higher and large parts of the middle classes have borrowed to invest in the bubble.

David Levy of the Jerome Levy Economics Institute in New York gives the following picture of how an uncontrolled expansion of fictitious credit money and of speculative forces in the US stock market were sustaining the US boom as of the start of 1998. In 4 of the last 5 years, consumption has grown faster than personal income. This has been a key factor in widening profit margins. In 1997 the personal savings rate in the US was at 3.8%, a fifty year low. A consumer borrowing boom helped spending outpace income in the mid-1990s, but by 1997 households faced record debt and debt service burdens. Households are carrying an unprecedented 85cents of debt for every dollar of after-tax income. Credit card delinquency rates are hovering near the previous all time high and personal bankruptcies keep breaking records. "Euphoria over stock market gains has powered the consumption spree." Consumers

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[151] David levy: Praying for a soft landing. Financial Times 2nd January,1998,page 10.

[152] Gerard Baker: Is This Great, or What? Financial Times, 31st March,1998, page 25

[153] Barry Riley: An Old Bull that Won't Die. Financial Times, 3/4th January 1998.

[154] Richard Waters: Where the Money is. Financial Times, 31st December,1997.

[155] Paul Krugman: Pity Alan Greenspan, Financial Times, 3rd June,1998, page 18

[156] William Dudley:From Virtuous to Vicious. Financial Times, 6th May,1998,page 18

have been spending not only in response to portfolio gains but also in anticipation of future gains. “Never in the post-war period have consumers been so influenced by the stock market.”

Stock market speculation has also done its bit for what President Clinton considers to be his greatest domestic achievement so far: getting on top of the US budget deficit. Capital gains tax receipts to the Treasury are up from $44bn in 1995 to $100bn for 1998: a direct indicator of the volumes of speculative trading in US securities markets.

But by the end of October 1998 the signs of a mounting financial crisis were multiplying. A credit crunch had already started in the US financial system. Institutions in debt were not able to find easy access to new credit. If the credit crunch were to spread to Main Street, demand in the US economy could collapse very swiftly. In short, the American people are, at the time of writing, at risk of being swept into the vortex of a crash generated by the speculative boom which they had hoped signalled a better future.
When the American central bank, the Federal Reserve Board, intervened in late September 1998 to save the Long Term Capital Management Fund (LTCM), it threw a beam of light into the black hole at the heart of what has come to be called globalization. Federal Reserve Board Chairman Alan Greenspan was issuing a simple, clear set of messages: that, since the Fed steps in only to tackle ‘systemic risk’, the safety of the entire American credit system was apparently threatened by the behaviour of a single, speculative Hedge Fund; that the international constellations of financial markets revolving around their American centre were in fact subordinated to a centre of speculators; that the welfare of literally billions of people, whose livelihoods depend in one way or the other on the functioning of credit systems, was potentially jeopardised by a couple of Nobel Prize winners and a former deputy chairman of the Fed who had been engaged in an orgy of reckless speculation; that the macro-economic policies of the rest of the world should be shifted by lowering interest rates to help bail out a Cayman Islands company. Globalization had come to this.

And while we were absorbing this set of messages, Greenspan proceeded to supply some more: he did not start moves to wind down and close LTCM. He also rejected an offer from a big mid-Western speculator, Warren Buffet to take the problem off his hands by taking it over. Instead Greenspan brought all the biggest American investment banks together to jointly run LTCM indefinitely, creating the mother of all speculative institutions. This prompted the Chairman of the House of Representatives Banking and Financial Services Committee, James Leach, to remark:
“Working as a cartel, those running LTCM potentially comprise the most powerful financial force in the history of the world and could influence the well-being of nation states for good or for naught, guided by profit motive, rather than national interest standards.”[157] Leach was right, as we already knew by the autumn of 1998. A handful of American institutions like LTCM had already demonstrated their *capacity to engage in full-scale financial warfare against states*. They can plunge a state into economic ruin, leaving tens of millions of people utterly destitute. And as Joseph Stiglitz, chief economist at the World Bank pointed out, many smaller economies in the world can be ruined in this way, regardless of their so-called ‘fundamentals’: their fundamentals are not as fundamental as these hedge funds.

[157] Quoted in Garth Alexander: ‘BankAmerica joins hedge fund casualties’, the Sunday Times, 18th October,1998, 3.9

Most of the biggest of these speculative organisations are completely opaque and unregulated because Alan Greenspan and US Treasury Secretary Robert Rubin (who comes from an organisation that derives about half its total income from speculative trading -- Goldman Sachs) have wanted them kept that way. This was his last message during the LTCM crisis: he claimed that such hedge funds could not be regulated because if they were, they would only escape to places like the Caymans! Instead, he proposes to make *the targets* of some of these organisations -- the financial systems of countries in the South -- much more transparent. As a Financial Times editorial remarked, this will simply make them even more vulnerable to speculative attack.

It is painful for mainstream economists to face this bizarre reality. We know that if a big bank at the heart of a financial system goes bust, it can pull down other banks through its defaults on debts and it can cause panic amongst savers when they see deposits in the bank being wiped out. But a speculative trader on securities markets or foreign exchange markets is surely something quite different. These operators are speculating in the sense that they are making profits through betting on price movements in a market or price differences between two markets. We know that such speculative activity is endemic in stock markets, bond markets and foreign exchange markets as well as in the so-called derivatives markets -- markets in instruments ‘derived’ from these more basic markets. But we take speculation to be the froth on the top of markets which are playing an indispensable role as ‘capital markets’ which help to ensure that capital goes to the most profitable sectors and places. So if a speculative operator bets wrongly and goes under, this should neither affect the underlying operations of these markets, which supposedly largely reflect real trends in economies, nor should it have anything to do with the banking system which is engaged in supplying credit to governments and the corporate sector.

Yet Greenspan’s rescue of the LTCM revealed a different picture. It has turned out that top American banks have been pouring enormous loans into speculative hedge funds and doing so without being interested in knowing anything about the bets which operators like the LTCM were engaged in on international financial markets. More, the Federal Reserve Board must have known for years that this had become a central feature of the activities of the core institutions of the US banking system. A one-line bill in Congress could have banned such lending but no move whatever was made by the US government to take such action. Thus we come to some inescapable conclusions: that for the leaders of American finance and of the US state, gigantic speculation on international financial markets was basically safe. Second, that it was extremely profitable. Thirdly, that it was a rational way to relate to these international financial markets. And fourthly, that it was good, in some way or other, for the health of American business.

These propositions could be minimally true only if the summits of American finance engaging in this speculation could, in some way or other, rig the markets. This, at first seems improbable. It would require some or all of the following conditions: that they had enormous market power, huge mobilised funds that could dictate short-run price movements in these markets; but if they were competing against each other they could cancel out each others’ attacks; so a second condition could be that they worked together, either by carving up markets into different spheres or by co-operatively entering a given market; a third possible condition also existed: that they could individually or collectively have access to insider information about future events on these markets, information that could enable them to win.

In LTCM's case, all three conditions seem to have been met. First, it was able to mobilise really enormous sums. IMF studies had indicated that hedge funds could mobilise loans amounting to 20 times there capital. But it turns out that LTCM could mobilise 250 times its capital of $2.6bn, in other words $650bn. This is enough to shake prices in any market. Secondly, LTCM turns out to be the instrument of a cartel of US investment banks, of *all of the top ones*, plus the biggest of the European banks, UBS, so competition was not a significant problem. And thirdly, it appears that LTCM had excellent channels to insider information. Congressman Leach pointed out that LTCM had links with governments. Italy's central bank has been a big investor in LTCM at the same time as it has been playing the Italian bond market! This is a startling revelation. Since the actions (and words) of the Bank of Italy can directly tilt prices in the Italian bond market, co-operation between the LTCM and the Bank looks like a winning, though criminal, combination. But that was not all. According to an internal report within Europe's largest bank, UBS, written in 1996, at that time no less than eight state banks were 'strategic investors' in LTCM. And the UBS report, a copy of which was obtained by Reuters, suggests there was collusion for it explains that LTCM's links with these state banks gave it "a window to see the structural changes occurring in these markets to which the strategic investors belong".[158] That is a polite way of saying LTCM had enough insider information to foretell the future. Is it any wonder that when UBS read that report, it decided to 'get a piece of the action'?

The final ingredient in LTCM's success was its public relations management. Journalists, academics or small time traders, reared on neo-classical theories of how financial markets work
might press the following question: since markets not traders set prices, how can a speculator like LTCM be sure to win? And LTCM's answer was, with the highest tech computer software designed by two Nobel Prize winning number crunchers!

The reality was that it would take a lot more than a power failure at LTCM's computer centre to put a stop to its winning run at the casino. Bringing down the mother of all hedge funds would require action by the mother and father of all 'exogenous shocks', the kind of shock, or series of shocks that hit the world in 1997-98. These shocks were not, actually, exogenous to the system that produced operators like the LTCM. They arose from the evolution of the inner dynamics of what has come to be called 'globalization'.

Globalisation's Dialectical Twist

The revelation that the summit of the US financial system consists of a handful of speculative hedge funds supplied with almost limitless credits by the American money-centre banks indicates that globalisation has worked itself out in a dialectical fashion over the last quarter of a century. It began in the heady days of the Nixon administration as a liberation of US economic management from the constraints of subordinating the American economy to the global economy of the Bretton Woods regime. International financial liberalisation did indeed increase the leverage of the American state over international economic affairs. But

[158] Ibid.

this expanded ***political freedom*** to manipulate the world economy for US economy advantage has ended by deeply distorting the US economy itself, making it far more vulnerable than ever before to forces that it cannot fully control.

Washington's capacity to manipulate the dollar price and to exploit Wall Street's international financial dominance enabled the US authorities to avoid doing what other states have had to do: watch the balance of payments, adjust the domestic economy to ensure high levels of domestic savings and investment, watch levels of public and private indebtedness, ensure an effective domestic system of financial intermediation to ensure the strong development of the domestic productive sector. The DWSR provided an escape route from all these tasks. And as a result, by all normal yardsticks of capitalist national accounting the US economy has become deeply distorted and unstable: unprecedentedly high levels of public and household debt, a deep structural balance of payments deficit and a business cycle dependent upon asset price bubbles.

And to keep the US economic show on the road, the United States has become deeply dependent upon Wall Street financial markets' ability to maintain huge inward flows of finance from all over the world. If these inward flows of funds were to come to a halt, or go into reverse, the structural weaknesses of the US economy would be starkly revealed, with potentially catastrophic consequences. In the jargon, Wall Street is a 'liquidity-driven' market whose constant resupply of funds from abroad plugs the hole of the US economy's low level of domestic savings and keeps the US domestic boom going.

This structural pattern means that American governments have acquired a vital interest in maintaining an international pattern of monetary and financial relations which is extremely volatile , unstable and crisis-prone, because it is these features of the international economic system which maintain the vast inflows of funds into New York. And it is in this context that we can see the way in which the big US hedge funds are not an aberration but are rather financial institutions in the (Deeply distorted) American national interest. Every international act of hedge fund financial warfare in any part of the world acts like a shot in the arm for the liquidity of the US financial markets, maintaining downward pressure on interest rates and stoking the stock market boom.

This dialectical twist of globalisation has not been the product of some planning unit in the American federal government. No evil group of conspirators sought to construct a system in which the macro-economic health of the US economy required monetary and financial chaos to be perpetually recreated in the international economy. The whole pattern is the result of a chain of blundering gambles. But the pattern remains, nonetheless, a structural one.

It is also, ultimately an unsustainable one, if for no other reason than because the US economy depends not only upon constantly reproduced international monetary and financial turbulence. It also depends increasingly upon expanding economic growth, especially in the so-called 'emerging markets' of Latin America and Asia. The US productive economy is ever more open and ever more dependent upon macro-economic developments in these economies. And thus does Washington find itself in a vicious contradiction: the US domestic economy depends upon Wall Street which depends upon chaotic instabilities in 'emerging market' financial systems; but at the same time the US domestic economy depends upon growing 'emerging market' economies able to absorb US products and generate high streams of profits for US companies operating within them.

CONCLUSIONS

The main argument in this essay has been that the central features of what has come to be called globalization have been, in the main, the consequence of deliberate decisions of the Nixon administration taken in order to secure the continued dominance of American capitalism within the capitalist world. While the original spur to the creation of the DWSR was a perceived threat to US dominance from Western Europe and Japan, the most malign consequences of this regime have been inflicted upon the populations of the South and on those of the former Soviet Bloc. They have paid for the regime through appalling financial and economic crises which have had devastating consequences for hundreds of millions of people. Today it is the turn of tens of millions of people in Indonesia who are experiencing the effects of this barbaric regime.

The DWSR's disastrous economic consequences for the majority of humanity have at the same time been accompanied by astonishing political success. Every financial and economic blow-out has been successfully blamed upon its victims and has been used to destroy the earlier development strategies of countries plunged into crisis. Whatever the weaknesses of earlier strategies, whether in Latin America or in Asia or in the former Eastern Bloc, their results were at least less damaging to the health and welfare of the majority of their populations than is the case under the frameworks devised by the US Treasury and transmitted through the IMF and the World Bank.

At the same time, what began as part of a battle by the Nixon administration against its triadic 'allies' has become increasingly a joint project of Atlantic capitalism -- the US and the EU -- against the rest of the world. We have made no attempt to investigate the underlying causes of the long stagnation in the advanced capitalist countries, but a growing theme in the 1980s and 1990s has been the formation of an Atlantic coalition for a new drive Southwards, using the DWSR to re-engineer social systems outside the core in order to co-ordinate them with the interests of Atlantic capitalism. This campaign should not be seen as being driven by a single compulsion, such as the search for cheap labour or the search for markets. It is better viewed as an exploitation of power over the international political economy by the US and the EU in order to extract every possible useful advantage through re-engineering societies outside the core; or, to put matters the other way round, to expel as many problems as can be expelled outwards from the core societies. Financial crises in the South, dependencies on US and EU markets, inherited debt burdens, inabilities to steer economies in the face of bewildering changes in the international economic environment -- all these factors have been seized upon by the Atlantic powers as instruments for gaining positions in the countries concerned: for seizing control of product markets, for buying local company assets to centralise capital under Atlantic control, for exploiting huge pools of cheap labour (shut out by ever stronger immigration barriers from access to core economies), for taking effective control of financial systems for speculative purposes, gaining higher marginal yields for the pension funds of the populations of the North and for engaging in orgies of speculation and frequently corruption and criminal activities. Most of these activities are presented as the very opposite: as teaching the supposedly ignorant and incompetent governments of the South how to run their affairs properly, as helping them to pay off debts, as supplying them with aid through FDI etc.

The pattern of Japanese capitalist expansion has been different in the 1980s and 1990s simply because Japanese capitalism has been far more genuinely productive as a national capitalist system than the capitalisms of the Atlantic world. While the bulk of so-called Foreign Direct Investment in Eastern Europe or in the South by Atlantic capitals has been a matter of taking over companies and market shares, Japanese capitalism's huge surpluses of value have been channelled into the creation of new productive assets in East and South East Asia and have been compatible with very rapid rates of growth and substantial industrial development in the region. The rapacious mercantilism of so much of the EU's trade policy towards the South and towards East Central and Eastern Europe and the drive of the US to compensate for competitive weaknesses in its productive sectors through taking predatory advantage of its monetary and financial sector dominance has contrasted with the Japanese capacity to stimulate and feel comfortable with rapid growth in East and South East Asia. But the result of the combined dynamic growth of China and the rest of the East and South East Asian region, in relative harmony with Japanese capitalism has been a perceived threat to the future dominance of the US over the world economy, a threat-perception fully shared by the West Europeans. The result was the gamble of the Clinton administration culminating in the so-called Asian crisis of 1997. The direct target of that gamble was the countries of East and South East Asia. But its indirect but more fundamental target was the possibility of an emergent regional bloc centred economically in Japan but potentially including China as well.

There is, as yet no conclusive evidence that Clinton Administration acted strategically from 1995 to use the dollar price rise, pressure to dismantle controls on the capital account, inflows of hot money and financial warfare by the US hedge Funds to bring countries in East and South East Asia to their knees. There is much circumstantial evidence to suggest strategic planning. But the question remains open. What is not in doubt is that once the hedge funds had struck, the US Treasury launched a dramatic assault against the social relations of production in South Korea with the aim of achieving a gleichschaltung of Korean assets and US capitalism.

But the very success of that assault was too much for the scarred tissue of the political economies of the rest of the periphery to sustain. Those wounds inflicted by earlier triumphs of the DWSR, in Russia and other parts of Eastern Europe, and in Latin America had not healed sufficiently to withstand the strains from the East Asian crisis and the resulting panic of 98 revealed the heart of globalization to be an extraordinary black hole of rampant Wall Street speculation. The G7 package of so-called reforms of the international financial system is nothing more than an attempt to keep the whole speculative show on the road.

It may be thought that the US government and the European Union are seriously campaigning to dismantle all controls on capital accounts and to completely open all economies to the complete freedom of movement of all forms of core capital at all times. It they were attempting to do this it could only be described as lunacy. Their aims have been much more limited, namely to gain ***the right*** to open up any economy as they please and to use multilateral treaties as a basis for laying siege to any political economy whose government is attempting to protect assets against capture by powerful Atlantic capitalist groups. The Atlantic powers have to balance their thirst for control over markets and assets and pools of labour against their need to preserve the stability or at least the viability states and political economies outside the core.

There are many in the Atlantic world and elsewhere who would hope, for the best of reasons, that the political fragmentation of the world into a balkanised patchwork of states could be overcome by steps towards genuine world government. This would, indeed, be a desirable goal. But it would be a grave error to assume that the current IMF/WB structures are a genuine step in that direction. The reality is that these structures are less genuinely supranational in their functioning than they were under the Bretton Woods regime and are far less so than was envisaged by Keynes and Dexter White when they negotiated the Bretton Woods regime during the war. What is overlooked by the proponents of developing these institutions further along their current lines is the fact that the principal obstacle to the construction of genuine organs of global governance lies in the most powerful states themselves. It is they who have the most to lose from such a development because at present they control these multilateral organisations for the purpose of furthering their own power and interests. And the entire IMF/WB system is designed to shift the costs of the power-plays of the Atlantic world onto the bulk of humanity, which lives in the South.

It is dispiriting for many to have to face the prospect of returning managerial autonomy to nation states in order to advance towards a more genuinely unified world. It might be thought possible to envisage a coalition of medium-sized states being formed to take dominance out of the hands of the United States government and organise a system of global governance which is at least based upon a broader kind of oligarchic co-operation between, say, the largest 20 countries (largest, that is, in population terms). This could be seen as a genuine step forward. But simply to state it is to see how distantly utopian such a programme of reform currently is, despite the fact that the Atlantic powers could still have the initiative within such a forum on most issues. They are addicted to maintaining their grip on the world economy and world politics, come what may.

Relations between the capitalist core and periphery have undergone extraordinary transformations during the 20th century. In many ways the optimal form of the relationship from the angle of core economies was that of the European Empires, with the British relationship to India being the paradigm. The inability of the core states to handle their own internal relations during the 20th century produced paradoxical results. The combination of two devastating European wars and new, far more productive American production technologies generated a new phase of post-war growth in the core. And the rising American capitalism needed to break-up the European empires rather than build a new exclusive empire of its own. But with the return of stagnation in the Atlantic economies, it has been the United States which has felt itself to be in need of a functional equivalent of Britain’s Indian Empire: a large source of cheap inputs for US industry and a vital destination for ever larger shares of US exports and local market control, and one that would, in addition, pay for its own administration and, like 19th century India, pay a handsome tribute to the imperial power. All these requirements have been sought by the US using the DWSR and the social engineering activities of the IMF/WB during the 1980s and 1990s.

Japan in the 1980s and 1990s, like the US at the end of the war, has had no need for such an imperial system: it could have sustained continuing and expanding growth in its region of the world, sorting out minor difficulties like a property bubble in Thailand, currency misalignments etc without significant difficulty. But it could have done so only if the US had been so locked in conflict with the EU as to have let Japan carry on without disruption.

The determination of successive US administrations since the 1970s to put America first has derived from the rational appreciation of the enormous privileges and benefits which the top capitalist power gains from being on top within an international capitalist system. But the struggle for power between capitalist states can no longer be a zero-sum game. This is not because the United States needs a booming Japanese or German economy for the prosperity of the American people. American leaders would be happy to accept slower US growth of say 1% per year for 5 years in exchange for Japanese growth of -1% per year for 5 years, rather than have US growth at 3% in exchange for Japanese growth at 5%. The real basis for inter-capitalist co-operation lies in the increasing difficulty the leaders of all three parts of the triad will have at managing an increasingly unruly world. This is the truth that has been temporarily eclipsed during the first Post-Cold War phase but remains fundamental for any sober political leadership.

As this essay has suggested the United States and the other Atlantic powers seek to strengthen their grip on other parts of the world mainly by capturing powerful social constituencies within the political economies concerned. There is a basis for such social linkages in the rentier interests among the dominant social groups outside the core. The reductio ad absurdam of such interests has been the class of predatory money-capitalists that was enabled, with great help from the Western financial sector, to seize control of the Russian state. But throughout the world, powerful rentier groups can enjoy great benefits from the ability to move funds out of their state into New York or London and thus insulate themselves from social breakdowns and developments within their own countries. These money-capitalists can also benefit from IMF/WB regimes which entrench the dominance of local financial sectors over political and economic life. And for rentiers it matters not in the slightest whether their royalties come from local business or from transnational corporations: if anything, the latter would be the preferred option.

The 1990s has been a very peculiar moment. During this decade, it appeared that labour as a social force had vanished for good. Into this momentary vacuum came what will, in future, be looked upon as a bizarre international social movement, the neo-liberal globalization movement. Many may believe that this movement was created ab initio by the American mass media. But it was created at least as much by the yearning of tens of millions of people throughout the world to hope that somehow the collapse of Communism would lead to a better world. In parts of the world like Eastern Europe, people simply had to believe such a thing in order to cope with cognitive dissonance. The result was the most absurd infatuation with diseased, speculative international financial markets and with equally absurd Washington Consensus nostrums about development through deflation leading towards depression. Whatever the outcome of the Panic of 98, this international social movement is intellectually finished. It is shrinking before our eyes into a narrow ideology of rentiers and speculators. They remain, of course, extremely powerful, but they have lost the capacity to present themselves as the bearers of any modernisation programme for the planet.

In the next phase of development the energy and elan of the rentiers will decline and labour will begin to regain its balance, despite the efforts of the World Bank and the financial sectors of the West to subordinate labour to rentier interests by destroying public welfare provision and introducing the euphemistically named ‘social safety’ net for the deserving destitute under private fund management. The long battle will begin to rebuild a modicum of public control over economic life and the social welfare of the mass of the populations of the world.

Is There an Alternative?

The Dollar-Wall Street Regime has tended to produce a new Atlantic alliance, shown in action for the first time in a really dramatic way during the East Asian crisis. In relation to strategies for organising the world economy there has been sufficient common ground between the US, Germany, British and Dutch capitalisms to design common programmes for advancing mutual interests internationally. Yet the creation of the Euro casts doubt on the political sustainability of this alliance. Independently of the intentions of EU leaders, the Euro could undermine the capacity of the US to maintain the DWSR quite quickly. The result of this development could be serious transatlantic strains, strains that will tend to be all the greater if they occur in a context of international economic stagnation or worse.

On the other hand, the Euro is coming into existence in an extraordinary political and institutional vacuum. There is, for example, not even an obvious institutional mechanism for running the Euro's exchange rate policy towards the dollar. And the likelihood of any genuinely democratic leadership over the economy of the European Union looks extremely remote, since to create one would require unanimous agreement from all 15 EU governments. It would appear, indeed, that there is a strong will to prevent democratic and accountable leadership from emerging. If so, this is another way of saying that speculative and rentier interests in the financial systems of the EU -- the social groups with the strongest links to their Central Banks and to the European Central Bank will exert predominant influence and will seek a close alliance with the United States. There is a widespread assumption in Western Europe that somehow the European Union is bound to have a more 'civilised' attitude towards the IMF/WB and the countries of the South than the attitude of American administrations. Yet evidence for this is almost impossible to come by, and at least as far as the general approaches of British, German and Dutch governments have been concerned, their record in the 1980s and 1990s towards North -South economic issues have often been worse than that of US governments. And in trade policy, the European Union has had an increasingly strong emphasis on neo-mercantilism, achieving maniacal proportions on occasion, partly, no doubt because of the European Commission's desire to prove itself valuable to member states by responding enthusiastically to almost any call for protectionist measures -- an attitude which is very understandable since the Commission as yet lacks any democratic credentials and must thus constantly prove its value as an instrument in the main policy area where it wields power -- that of trade policy.

Nevertheless, the arrival in power of the German Social Democratic government alongside the Socialists in France and the PDS in Italy, may give hope for a change of direction in EU policy. It would therefore seem possible to imagine a change of orientation at the level of the Council of Ministers. If so, it is not very difficult to propose measures which would help to tackle many of the malign developments which are grouped under the name of globalization.

A first step would be an end to the attempt to extend the power of the dominant capitalist powers over the conduct of economic and social policy in other states throughout the world. The EU should simply declare that all states should have the right to decide how they wish to manage their financial systems, what controls they wish to have on their capital accounts, what rights they wish to provide for or deny to multinational companies, financial services etc. and indeed what trade policies they wish to pursue. The EU may wish to continue to accept all the international obligations it has entered into with the US in the WTO, the OECD,etc., but it would oppose attempts to brigade other states into accepting these regimes and it would oppose attempts to exclude states from the application of GATT principles because they did not wish to subscribe to this or that liberalisation programme. Secondly, the EU should declare that financial institutions lending internationally must be supervised and protected by their home governments, who should bear the full costs of bailing them out. The IMF will provide bridging loans to such governments to help them bail out their banks, hedge funds etc. but their tax-payers must ultimately foot the bill. Thus, if US banks or hedge funds are facing collapse through a payments crisis either at home or abroad they must turn to their domestic lender of last resort for help. They should no longer expect the poor of Indonesia or Brazil or Russia to foot the bill. Thirdly, lenders must understand that sovereign governments have the right to unilaterally repudiate debt. This is a risk that lenders must build into their calculations when lending funds abroad. Fourthly, the EU must take steps to initiate a new system of public EU insurance of loans to other governments whether made by EU private or public financial institutions on the basis of EU approval of the purposes of these loans. Such loan insurance operations should be transparent and democratically accountable. All other private lending activities abroad would not be covered at all in the event of borrower default. And finally, the EU would *temporarily* continue to participate in current IMF/WB operations but only on the understanding that all IMF/WB conditionalities would be published and on the basis that an international conference was convened to reorganise the international monetary financial system in line with recommendations such as those suggested here. If such ideas were not adopted by the other main powers, the EU should adopt a policy of international pluralism in the handling of international economic management. Those states which desired to continue within the IMF framework would be free to do so, while other states might prefer to operate within the EU framework. At the same time, the EU would seek to negotiate agreements with other countries establishing regimes of fixed but adjustable exchange rates.

Proposals of this sort should be combined with the reassertion of an EU financial system centred on bank intermediation of finance, strong public regulation and a preference for public or co-operative saving institutions. The tax systems of member states should be adapted to ensure the taxation of flows of hot money into and out of the EU and to ensure that speculative trading on securities markets was penalised through taxation. Tax havens should be abolished throughout the EU and the EU should work to eradicate them internationally. One way in which this could be done would be through ensuring that information about persons or companies maintaining funds offshore are made available to the relevant tax authorities within the EU and such persons or companies should be made liable for the payment of taxes on these funds in their EU country of citizenship.

For some such reform programme to be carried through would require a very substantial exercise of political power over rentier and speculator interests within the EU itself. The speculators often try to claim that a reassertion of public control over international finance is technically impossible because of technological change. But these claims have force only in the sense that it is technically impossible for states to prevent crimes. This is true: most of the work of the judicial system is ex post facto: first the crime, then the investigation and prosecution. It is the same in the case of private international finance. Regulators cannot stop companies from switching funds around the world, legally or illegally. But they must be able find out what has been happening after the event. If they cannot do so, then this is because the top managements of the companies concerned cannot themselves find out what their operational staff have been doing with their funds. Of course, managerial controls are often poor -- witness Barings and many other similar disasters. But if managements can keep records of what their companies have been up to, then states can keep track of what has been happening through the usual requirements for 'transparency': they can inspect the books. Of course, they cannot do so 100%: there will be a great deal of fraud and corruption at the very top of the financial system. But states can still exercise great sway, if they have the political will to do so.

But the problem of mustering political will to re-subordinate money-dealing capital to public policy goals for economic development lies at bottom in the area of strategies for economic revival. What gives the private financial sector its social and political dominance is above all economic stagnation. Under conditions of stagnation, governments go into fiscal deficits and public debt mounts. This makes governments dependent upon conditions in bond markets. The private financial operators demand deflationary retrenchment of public finances, thus deepening the cycle of stagnation and rentier dependence. A strategy for re-imposing public order over economic and social life thus depends upon combining such measures with an economic growth strategy.

This brings us to a fundamental question has been deliberately avoided throughout this essay, namely the causes of the long stagnation in the production systems of the core over most of the last quarter of a century. We will not begin a serious exploration of that issue here. But most ways of explaining the reasons for the long stagnation would tend to do so by suggesting that there has been some sort of saturation or overproduction crisis within the triadic economies. If that is the case, then given the right environment, there should be the possibility for a dynamic process of catch-up development in the new regions opened up to capitalism in East Central and Eastern Europe, in other words for these economies to play the role of a catch-up growth centre which had been played by East and South East Asia. If such a catch-up growth were to take place, it would not resolve the deeper historical problems of the stagnation, but it would substantially ease them.

During the 1990s, this potentiality in East Central and Eastern Europe has been squandered by the combined efforts of the capitalisms of both sides of the Atlantic to engage in short-term predatory tactics towards the region. The United States has been obsessed with integrating the region into its dollar-wall street regime for international monetary and financial manipulations, without the slightest interest in the establishment of favourable conditions for regional development. While West European governments, mired in stagnation and internal social and political tensions, have viewed the region basically as a source of problems and political-economic threats: a source of pressures for the restructuring of industries in Western Europe, a source of population migration threats and a source of budgetary threats if a country like Poland were to enter the European Union. No serious international strategy for the economic revival and for the economic development of the region has been attempted.

The obvious place to begin the search for such a strategy is in Western Europe amongst the parties of the Social Democratic Left. For fifteen years European Social Democracy has been a political nullity, with its leaderships in France, Italy, Spain and Belgium sharing as much in common in the field of direct financial corruption as in anything else.As for Blair's labour leadership it is bought and paid for. But the new German Finance Minister, Lafontaine, is certainly different. He is a determined European keynesian with a strong will and a political following in a political economy that is absolutely central. This raises the possibility of a keynsianism not so much rooted in the Keynes of redistributing income within a national economy to boost effective demand -- although such redistribution would be a good thing in itself -- but in the Keynes of ideas for organising the post-war international economy for growth: the Keynes who sought to propose the kind of 'financial repression' and statist development strategy for the world, placing productive growth in the saddle and organising euthanasia for the rentier -- a model that is now rather bizarrely thought of by many as an East Asian invention.

I think that this is a theoretical possibility. Just as capitalism found a way out, in the end from the crisis of the 1930s and the war, a way out that offered a greatly improved deal for a large part of humanity, so I believe it could, in principle, do so again. But I doubt that it will, not because of the nature of capitalism as such, but because a solution would require a *tactical radicalism* and an intransigence of political will which it is difficult to imagine European social democracy as being capable of.

A European Social Democratic answer to the present crisis, led by the new German government, would have to take very bold steps with the support of other governments like those of France and Italy for a pan-European strategy for economic revival. The key to such a strategy must be to tackle the payments weaknesses and vulnerability of the East Central and East European economies. This is where the Euro could be used as a powerful lever, backed by the financial power of the ECB. With the arrival of the Euro, the member states of Euro-land will no longer have to worry about their current account balance because they won't have one. They should therefore become less mercantilist about trade issues. Secondly the Euro will give seigniorage privileges to Euroland in the East. The latter economies will denominate their trade, their accounting, their reserves in Euros. Euroland can buy as much as it wants in the East and just pay for everything in the currency which they produce: Euros. Euroland can do for the East what the USA did for Japan after the war: open its market wide.

But that is not the most important way in which the Euro could be used. The vital task is first to secure the currencies of the East against speculative attack so strongly that they can greatly enlarge their current account deficits without worries about the sustainability of these deficits. This task of securing their currencies is not a significant problem for Euroland's Central Bank because of the enormous financial resources in its hands, now dwarfing tiny banks like the Bundesbank. The bundesbank offered guarantees of unlimited very short term support for the Franc. The ECB can with ease offer the same only much more so to the currencies of the Eastern region. These governments can then forget their worries about hedge funds and ignore the IMF. And even if Euroland does not impose new capital controls, it should certainly urge East Central and East European governments to do so, so that Wall Street can never 'short' their currencies in the forward foreign exchange markets again. The Euroland authorities could declare that for a five year period they are aiming for the states of East Central and Eastern Europe to run trade deficits of 10% of their GDPs and the ECB will underwrite their currencies while they are doing so. Secondly, these economies should use their deficits for infrastructure projects and investment in fixed capital projects of their choice. They will have the resulting deficits funded out of the current very large trade surpluses of the EU (or Euroland).

This means large, serious, very long-term credits or even grants (funded through a 'tax' in the EU current account surplus . They do not have to be at non-market 'aid' rates although they could easily be. But they must be long-term and big and should be handled by public authorities in Euroland. The US and European investment banks, speculators and rentiers have already had their sport in the Eastern region. It is now time to clear out their augean stables. Either large public offerings of long term bonds issued by the European Investment Bank or long-term loans to the region offered by the same bank (actually a bank made up of the states of the EU) should be advanced.

These mechanisms could at last begin a virtuous circle of productive inter-action between the two halves of the continent. The East could import the plant that it needs and expand its domestic markets and exports West. The expanding streams of income in the east could provide the effective demand for expanded imports from the West. Speculative fevers could subside across the continent and full employment could return, aided no doubt by Lafontaine style large transfers of wealth back from capital to labour through the tax system. If big capitals in Europe still wish to emigrate, let them go. But where to? From the biggest integrating market in the world to the shattered tissue of economies in the South being managed under intellectually bankrupt 'development models' of rentier capitalism 'liberated' from the 'financial repression' that served the capitalist world so well in the days of the Communist threat.

If the new German social democratic government in Germany could embark on a path like that and largely pull it off, then Euroland could begin to offer a way out for other parts of the world as well. But it would be a bitter political battle against enormously powerful financial interests which have thrived on the DWSR and which have the strong support of the US government. It is a course that would wreck the international strategy of American capitalism challenging its entire ideology. It would require the German social democrats to build a ***political coalition*** across Europe and one that could genuinely fire popular enthusiasm. And such a coalition would, if necessary, have to be prepared to break the great taboo of the entire Cold War period: it would have to be prepared, if necessary to mobilise public opinion in Europe *against* the American ally, simply in order to defend the strategy against US disruption. And those who have followed the Bosnian crisis closely know how far the US is prepared to go when high political stakes are involved. So do those who have followed the East Asian crisis closely.

But the major impediment to such a strategy lies not within the United States or with the social power of rentier interests. It lies in two other directions: first, in the deep nationalist subordinations of the Social Democratic Parties of Europe themselves. A plan for West European revival through a Marshall-type plan for East Central and Eastern Europe would be viewed in Paris (or London) as a plan to strengthen Germany rather than France or the UK. This would be the first stumbling block. The second would be that there is no effective institutional structure for actually pursuing such a plan: there is no economic government for Euro-land, no responsible democratic leadership for using the Euro as an instrument of economic revival and no easy path to achieving appropriate institutional mechanisms: gaining them would require an EU Intergovernmental Conference at which unanimity was achieved not just to supplement the Maastricht Treaty but to substantially modify it to make the ECB more like the Federal Reserve Board of the United States: an institution with the explicit task of serving socially useful development purposes. Such changes could be achieved. But the record suggests that they will not be. The Blair government, for one, would, on its past record, wish to play a wrecking role since Blair himself is a passionate enemy of what he calls the ‘tax and spend’ European social model. On the other hand, it could be argued that Blair is not really attached to any idea whatever, and might be won over to such a project of reform. Or alternatively the institutional mechanisms could be developed informally through the committee on Euro-land finance ministers from which the British government is currently excluded.

If the new German social democratic government and its social democratic partners in France and Italy cannot make the turn from national particularism and from the EU’s current orthodoxies of central bank supremacy and neo-mercantilist trade policy, the outlook for the future will not look hopeful, from a European angle. A centre-left American government project would possess most of the instruments for a more creative policy but there is no sign whatever of the American political system being able to produce a functional equivalent to German social democracy and at the same time the American state is too deeply mired in structural debt problems to be able to offer a new development strategy for the South through its own efforts.

In such conditions there will be only one choice for those, whether liberal or social democratic, to make if they are consequent in their thinking: they can abandon their liberal or social democratic values, for the sake of overcoming cognitive dissonance, and let the world slide into ever increasing dislocations and upheavals in which the most dynamic sector of all economies will be the insurance industry, thriving off the mounting dangers bred by spreading social disintegration. It will be a world marked by ever more destructive kinds of imperial gambles with the livelihoods of the bulk of humanity.

Alternatively, we can turn back once again to the task of building internationalist movements for world reform based upon a recognition that Marx was right about capitalism being ultimately incapable of providing a viable framework for sustainable human society on this planet.