

Monetary Policy: A Missing Element in the Global Marshall Plan Initiative?

James Bernard Quilligan

The Global Marshall Plan Initiative represents a significant breakthrough in multilateral economic restructuring, particularly because it establishes crucial links between international trade and finance, global environmental reform, and the eradication of global poverty. The weakness of the GMPI, however, is that it does not address the monetary instability which two of its primary proposals are likely to create.

Let's first examine the GMPI proposal for an expansion of the Special Drawing Rights of the International Monetary Fund and the creation of global taxes on international trade and currency transactions. Following the Zedillo report (the 2001 UN High-Level Panel on Financing for Development), the stated goal is to raise roughly US \$1 trillion by 2015 to supplement foreign aid in ending poverty and enabling poor nations to become economically self-reliant and to build new local markets, thereby creating a major stimulus for the global economy. However, on pages 145-46 of the Global Marshall Plan: A Planetary Contract, the authors suggest that US \$1 trillion *per year* in new revenues may be more realistic – roughly \$10 trillion overall by 2015, or 1.5% GWP annually – which is more in line with recent projections of the World Bank and International Monetary Fund for meeting the UN Millennium Development Goals. Granted that these increased levels of funding would be phased in, and that many other international economic factors are obviously at work, it is still fair to ask: how would these new multilateral funds for poverty relief and development impact the global currency reserve system? Under the present monetary regime, the American dollar is the currency that most nations use to buy oil, trade for goods and services, pay their short-term international debts, and hold in their Central Banks to protect their own domestic currencies from inflation or devaluation, ensure long-term credit, and attract foreign investment into the domestic economy. With the US current account deficit now at 6.6% of GDP, many economists already consider it unlikely that the US can continue to keep its inflation low without a major increase in interest rates. With much easier access to financing and credit through the introduction of SDRs and global taxes redistributed on a global basis for human and social development, the Central Banks of many nations would have little incentive to continue holding US dollars as the asset reserve for their domestic currencies. Confident that their governments will receive new streams of financing from SDRs and global taxes over a period of years, these Banks would move to reduce their dollar reserves. In reaction, many foreign investors would also unload their dollar debt by withdrawing their funding from America's credit-driven economy. As a consequence, the United States would be forced to (1) reduce its massive current-account deficit (its trade flows and other international payments) through a fall in the value of the dollar; and (2) increase its savings either through a significant decline in consumer and corporate spending or by slashing its federal budget deficit drastically. These two fiscal adjustments in the US would send shockwaves across the world, creating volatility in exchange rates and a disruption of global capital flows, access to credit, and currency stability. Thus, without a reliable international currency anchor to ensure long-term fiscal discipline, the anti-poverty and development funds generated by the proposed expansion of SDRs and the introduction of global taxes would flood the world with new revenue, depressing the world's reserve currency value and necessitating an overhaul of the global monetary system.

Second, let's consider environmental reform. Since the US untethered the world monetary system from the gold standard in 1971, no material resource of intrinsic worth is being used as a reserve base for the international money supply – or so it is claimed. Officially, in the US and elsewhere, paper currency is backed only by the people's faith in their government's sovereignty. But because oil is primarily priced in dollars across the world and has more direct influence on the value of currency than any other factor, the US dollar is fundamentally linked to global crude oil as its *de facto* reserve base. So when it sets interest rates, the US Federal Reserve is actually reacting to relative price stability caused by the global reserve and flow of petroleum as it affects US and global economic output and growth. Thus, it is the oil-driven engine of productivity in relation to the global oil reserve that the US Central Bank uses to determine the value of American currency and, by virtue of US dollar hegemony, the world's currencies. How would the global currency reserve system be affected by the GMPI proposal for major ecological reform? The GMPI acknowledges the need to internalize the external costs of environmental degradation and climate change into the market system by setting a real price on carbon emissions. The idea is that as consumers and businesses are forced to adjust their practices and lifestyles by reducing their oil consumption, and businesses find that investing in efficiency or alternative energy is cost-effective, they will absorb most of the new environmental costs through higher prices. While this formula gives primacy to the economic signals of the marketplace, it ignores the independent monetary driver of energy reserves, currency values, and interest rates. Any major shift by governments to price carbon emissions in market terms will result in a dramatic increase in oil prices, creating inflation, an increase in interest rates, fluctuations of exchange rates, upheavals in global capital markets, disruptions in access to credit, and volatility in the US dollar and international currencies tightly linked to the dollar. In addition, even if we begin to curb our appetite for oil, develop alternative fuels and achieve energy efficiency through technological advances, petroleum will continue to be the most important ingredient of economic productivity and growth, and the profit and wage incentives in these 'green' businesses will still be denominated in dollars that are linked directly to oil. Greening all of the world's businesses through the marketplace will proceed cautiously and will not change the energy base of civilization from fossil fuel to solar or other renewable energies until the world's oil supply is no longer used as the reserve standard of the dominant global currency.

The present monetary system cannot sustain an anti-poverty program that would depress the world reserve currency, or an environmental program that would inflate global prices, either singly or in combination. But that does not mean that the GMPI proposals are wrong. On the contrary, the GMPI proposals for development and environment are greatly needed and correct as far as they go. They simply need to be set in a broader monetary context that ensures they will work synergistically. This is especially important for global policy makers who are now considering these matters closely because the GMPI appears to underestimate the actual amount of total funds – probably \$1 trillion per annum – that will be needed to address global social and ecological problems during the next few decades. We need to be confident that major new economic reforms will be adequately supported by the international reserve currency system. If the Global Marshall Plan is to be seen as a realistic step toward the adjustment of global capital flows, leading to the creation of inclusive global governance, it must anticipate the end of American dollar hegemony and the dollar-based oil reserve standard, and concern itself with the reorganization of the international monetary system through a self-adjusting global balance of payments mechanism, allowing nations to cooperate through a system of fair trade exchange, equitable financial reciprocity, stable exchange rates, and the impartial distribution of multilateral

resources. One solution would be to create a new international trade currency based upon a basket of global resources (including a broad proportion of renewable resources, gold and other non-renewable resources), in which the value of currencies would rise when the reserves in this basket are scarce and fall when those reserves are more plentiful. Global currency value would thus be determined by the sustainability of global resources as monetary reserves – not by their price in the marketplace based on economic productivity and growth. Ultimately, the external costs of global poverty and the environment must be adjusted, not only through alternative sources of finance and market pricing, but also through an adjustment of the world reserve currency system.

As the Brandt Commission predicted in 1980, “Without clear rules to govern the conduct of monetary relations, governments could be more and more tempted to take unilateral actions – whether for damage limitation or for national advantage – that would lead to great political friction and growing nationalistic sentiments. There is thus an urgent need to establish a mutually agreed international monetary order which would take into account the changes in the world environment since 1944...The Commission believes that reform of the world monetary system...must address itself to the following issues: the exchange rate regime, the reserve system (the creation and distribution of the international means of payment or liquidity); and the adjustment mechanism as it affect the countries issuing reserve currencies, surplus countries and deficit countries.”

We know from history that no monetary system lasts forever. Sooner or later, a new system must evolve. The Global Marshall Plan Initiative is uniquely positioned to negotiate and influence that transformation.

James Bernard Quilligan is the managing director of Centre for Global Negotiations and US coordinator of the Global Marshall Plan Initiative.