The return of the bancor? Chinese ascendancy and the global monetary system

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ANDREW PICKERING, APR 12 2009

The global financial crisis has so far failed to yield a second Bretton Woods agreement, as some had hoped, but recent calls for a new global reserve currency are beginning to excite the minds of politicians, financiers and scholars alike. Taking inspiration from the 'bancor' currency proposed by John Maynard Keynes in 1944, the governor of the People's Bank of China suggested last month that the global monetary system would benefit from revamping the role of the International Monetary Fund's special drawing rights (SDRs) to create a uniform global reserve currency.[i]Arguing that the Triffin dilemma[ii] was at the root of the present crisis, Zhou Xiaochuan proposed that SDRs take on the role now played primarily by the dollar (and to an increasing extent the euro) as the reserve currency of choice.

These proposals reflect a new and growing boldness (debatably interpreted as intransigence) from the Chinese government, especially in matters of global finance. Catalysed by the current crisis, there can be no doubt that the communist regime feels that its moment as an ascendant hyperpower has come. In the run up to the G20's London Summit, it became clear that in the light of European disunity, the strategic dialogue between America and China would be decisive – both now and in the future. With Chinese investment in Africa alarming western diplomats, as well as widespread concerns over the alleged manipulation of the renminbi's exchange rate, China knows that it is in a historically unique position of power.

The idea that the current crisis can be blamed on monetary imbalances is hard to substantiate and most commentators are inclined to side with the position that toxic assets created a chain reaction resulting in a credit crunch. In reality, Zhou's concern stems from Chinese fears about the stability of the dollar, given that China holds reserves of over $1 trillion. Nonetheless, China's self-interest could have the side-effect of promoting a more equitable monetary system. George Monbiot has written on this subject in his book *The Age of Consent* and a good summary of his proposals appeared last year in *The Guardian*.[iii] Indeed, there seems little question that breaking the US dominance of the monetary system appears fairer on the face of it, but policy-makers are right to be concerned about implications for structural stability.

The hegemonic role of the US has depended on the role of the dollar as a global reserve currency – the greenback constitutes 63% of the world's reserves[iv] and it is this that allows the maintenance of the US's enduring trade deficit. But here we are faced with the inevitable dilemma of hegemony: however much the citizens of the world might resent the power of America, we will all miss it when it's gone.

That said, Zhou's idea has received warm welcomes from the three other BRICs (Brazil, India and Russia), as well as—surprisingly—a relatively supportive response from the United States. Treasury Secretary Timothy Geithner is quoted as being 'quite open' to the concept.[v] Some have seen this as a reflection of the multilateral rhetoric of President Obama, though it would be naïve to read too much into Geithner's comments at this stage. Other high-profile American supporters include the Peterson Institute's Fred Bergsten, who gave the idea a positive hearing in the *Financial Times* and former World Bank Chief Economist/globalisation guru Joseph Stiglitz, who has allied himself to the prospective changes.[vi]

There should be no doubt that those concerned with global justice are, broadly speaking, instinctively in favour a global reserve currency. Similarly, many also admire Keynes' idea of an international clearing union to manage balance-of-payments imbalances.[vii] All the same, it should be acknowledged instinct is not sufficient. Nowhere is the doctrine of unintended consequences as powerful as in matters such as this. Nonetheless, this is a critical discussion that is long overdue. Hopefully the debate will reflect that fact that there is more to this proposal than the same old contest between stability and fairness, if for no other reason than that—as governments and their citizens should know by now—systemic iniquity is inherently destabilising.

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[i] The People's Bank of China – Speeches, http://www.pbc.gov.cn/english/detail.asp?col=6500&ID=178, (Accessed April 9, 2009)

[ii] The Triffin dilemma is named for Robert Triffin, who realised that under the gold standard, American expenditure meant that quantity of dollars flowing out of the United States would sooner or later exceed the quantity of gold held by the US to back it up. The dollar was overvalued and since the US was unwilling to reduce the dollars in circulation, President Nixon ended dollar-gold convertibility in the so-called 'Nixon shock' of 1971. This meant the end of the formal Bretton Woods monetary system.

[iii] The Guardian, George Monbiot: Lord Keynes really did propose the International Monetary Fund, http://www.guardian.co.uk/commentisfree/2008/nov/18/lord-keynes-international-monetary-fund, (Accessed April 9, 2009)

[iv] International Monetary Fund, Currency Composition of Official Foreign Exchange Reserves, http://www.imf.org/external/np/sta/cofer/eng/cofer.pdf, (Accessed April 9, 2009)

[v] Reuters, Geithner says quite open to China's SDR proposal, http://www.reuters.com/article/businessNews/idUSTRE52O43O20090325, (Accessed April 9, 2009)

[vi] Financial Times, We should listen to Beijing's currency idea, http://www.ft.com/cms/s/0/7372bbd0-2470-11de-9a01-00144feabdc0.html?nclick_check=1; Reuters, New reserve currency could come quickly-Stiglitz, http://www.reuters.com/article/marketsNews/idUSN2650403720090326, (Accessed April 9, 2009)

[vii] For a concise explanation, see Wikipedia, International Clearing Union, http://en.wikipedia.org/wiki/International_Clearing_Union, (Accessed April 9, 2009)

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