
Amid the rubble of global finance, a blueprint for Bretton Woods II

The international financial system is broken. An integrated set of reforms will be needed to achieve sustained economic growth and shared prosperity. The G8 leaders of Europe, Japan and the US have agreed on an emergency summit this autumn in New York to revamp the international system - a good idea, provided it initiates a wide-ranging set of changes rather than being a one-off meeting focused on market regulation.

The G8 leaders are keen to start on regulation and that is understandable. Wall Street, the City of London and other financial centres ran wild with under-capitalised borrowing and lending stoked by over-the-top fees and bonuses. Alan Greenspan's Federal Reserve fed the financial bubble with rock-bottom interest rates and regulatory forbearance, when it had the chance to restrain it. And the derivatives market was allowed to become so vast and unwieldy that there is no clarity as to who owes what to whom in tens of trillions of dollars of credit default swaps and other derivatives.

Risk assessments have been made enterprise by enterprise without consideration of systemic risk. When institutions are «too big to fail», they must be closely supervised so that indeed they don't bring the entire system down when they do, from time to time, fail. And we have learned again that there is no global lender of last resort, only a hodgepodge of individual central banks and treasuries, whose individual actions may be sufficient or not to stem a panic.

The G8 leaders must go well beyond the issues of financial regulation, however. Even before the current crisis, the global economic system was failing in crucial ways. Many poor countries remain cut off

from global prosperity, often falling into poverty-induced violence and conflict. These will be still harder hit by the downturn. The global environmental crisis was also worsening, and climate shocks were wreaking havoc with world food supplies. Energy systems were in turmoil as the growing world economy pushed against supply constraints, yet there was no consensus on how to create an energy system compatible with the environmental and economic needs of the planet. These challenges are in desperate need of attention not only on their own merits, but also because global economic growth cannot be sustained without solutions to these crises.

Financial assistance to the poorest countries - a lifeline for more than a billion people - is in tatters. Europe and the US have mobilised around \$3 trillion in the past month in guarantees and bail-out funds for the banks but failed to mobilise even one ten-thousandth of that this year to help the world's poorest grow more food in the midst of a massive food-price increase and hunger crisis.

The US has been blind to the millennium development goals (MDGs) on fighting poverty, hunger, and disease. When George Bush addressed the UN in September - supposedly the mid-point in achieving the goals - he mentioned «terror» 31 times while failing to mention the goals even once. All the big donors except Britain - including the US, Japan, France, Germany, Italy, and Canada - are failing to live up to long-standing aid commitments.

The leaders should pause to reflect that there is another little-mentioned international summit scheduled for December in Doha, Qatar, to take up the challenge of financing development. It comes six years after a similar summit in Mexico, at which

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countries pledged «concrete efforts» to achieve 0.7% of GNP in development assistance - a level of aid none of them have yet fulfilled.

A true Bretton Woods II summit would set a financial framework to achieve urgent global goals in macroeconomic stability, economic development, environmental sustainability and trade for development. All these are vital for long-term sustainable growth, but global goals in all four areas remain unachieved. Summiteers should come with checkbooks and international commitments in hand.

Here, then, is an agenda for Bretton Woods II. First, we need to restructure global finance, based on an expanded system of capital adequacy standards, financial reporting, system-wide risk management, and new lender-of-last-resort capacities. Derivatives traders, hedge funds, and broker dealers would be brought under regulatory control. The IMF would be empowered to be a true global lender of last resort (as I urged a dozen years ago, warning of the threat of self-fulfilling panics). To make this possible, a small tax on financial transactions - a Tobin tax - would be implemented to expand the IMF's war chest in case of crisis and to fund other urgent international needs.

Second, the new global financial structure should help to rescue the world from human-induced climate change. A straightforward tax on the carbon content of fossil fuels, levied by all countries, would do the job, and much better than the enormously cumbersome emission-trading system concocted and championed by the same financial engineers who brought us our current banking crisis. Most of the carbon-tax revenues would stay at home in each country, to help finance low-emission technologies. Some would be directed to finance three global public goods: research and development on sustainable energy; transfer of sustainable-energy technology to low-income countries; and climate-change adaptation.

Third, the World Bank should be refocused with clear goals, and accountability for their success. Specifically, the bank should have one overarching assignment: helping the poorest countries achieve the millennium development goals to reduce poverty, hunger and disease. The bank is poorly organised for such leadership today. Like any bureaucracy, it avoids being held accountable for measurable results. With a tighter focus on the MDGs, the bank should also be supported with much larger financial resources from new revenue sources (such as the Tobin tax), so that the bank can better help the poorest countries expand vital infrastructure (power, roads, water, sanitation and broadband networks).

Fourth, the global trade agenda should be integrated with the finance, and environment objectives. The Doha trade round has failed because the world could not see any urgent reasons for its success. A trade agreement worthy of the effort would do two main things. Importantly, it would help the poorest countries to be more productive so that they can be full participants in the global trading system. «Aid for trade» would help these countries to build the skills, roads, bridges and clean power grids to support increased trade. In addition, global trade would promote environmental sustainability, to help enforce compliance with reduced carbon emissions and protection of endangered biodiversity.

All these reforms are vital for long-term sustainable growth and development. If the political leaders focus only on financial-sector stability, but neglect the long-term problems of energy supplies, climate change, food production, disease control and extreme poverty, then global growth might be restored in the short term, only to succumb quickly to another global bout of rising energy and food prices, and geopolitical instability.

The shortcomings of the existing Bretton Woods institutions, global environmental policies and international trading arrangements have been widely

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recognised for at least a generation. The current global crisis, and arrival of a new US president in the midst of this unprecedented economic meltdown, may finally mark the moment when the world takes seriously the urgent global economic and environmental agenda that confronts us in this new millennium. A summit in December will be a small step but could be the first meaningful action to steer the world to safety from the dire threats we face.

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