GLOBAL IMBALANCES AND THE DOLLAR

KRSTE SHAJNOSKI *assoc. prof. PhD*
MARGARITA MATLIEVSKA *assoc. prof. PhD,* STEVAN GABER *assoc. prof. PhD,* EMILIJA MITEVA KACARSKI *M.Sc*., ELENA NIKOLOVA *M.Sc.*

Abstract

For several years the issue of global imbalances has attracted the attention of the scientific and general public in developed countries and emerging countries. The authors of this article address different views on the causes of global imbalances and suggest that they more or less reflect the interests of actors in discussions in order to provide a painless solution to his country in addressing global imbalances. This is especially evident in discussions in which blame for global imbalances switches on underappreciated Yuan (China), or on excessive saving in emerging countries. The development of attitudes about the causes of global imbalances is due to the in sustainability of the argument previously imposed. The authors believe that contemporary global imbalance can not be explained without the internal causes of deficits and external debt of the United States, the weakness of the dollar.

There is no doubt that using the dollar as world currency is the cause of global imbalances because it generates growth in the current account deficit of the United States, and at the same time, these deficits are necessary to create sufficient liquidity worldwide. It is high time the national currency-the dollar, which performs the function of world money, to be replaced with real world currency. In this context the authors actualize proposal of J.M. Keynes to create the world's money (under the name bancor) because their mechanism of operation ensures the exchange equilibrium, without the occurrence of excessive deficits and surpluses in different countries. It establishes the principle of equal responsibility of the member countries of borrowers and creditors to maintain a balance in international payments.
Keywords: global imbalances, dollar, deficits, external debt, real world currency.
Jell classification: G01

Introduction

The causes for the global imbalance are the issues of numerous research. Still, more or less there are equaled on individual aspects, which obviously have the influence to the appearance and the development of the imbalances, but not the primary ones. This refers, for example to the disputes for the undervalued of the Chinese Yuan to dollar as a reason for the USA external deficits. Separately observed, as a cause for the imbalances might be treated the excessive saving in the developing countries, opposite to the neglecting of the saving and living on credits in the developed countries. But, these are only consequences of the international economic relations after the breaking down of the Bretton Woods system, after abounding of the gold exchange standard and the fixed parities in the intercurrence relations in the world that is after the abounding of the currency convertibility in gold and transfer in fluctuating exchange rates.

The real reasons should be searched in the abundance of the concept of the commodity money and in inauguration of the national currencies (primarily the dollar) in function of world money. These can be concluded from the function of the system of gold exchange standard (where the imbalances are temporary and they are overcome with the acting of the national economies according to advance confirmed rules). The positive effects from the concept of commodity money (in conditions of paper money systems) can be seen in the proposal of J.M Keynes for creation of separate money- bancors- which value would be expressed in gold and the currencies of the countries members its own value would confirm to bancor. The functioning of the proposed mechanism secures the balance of the countries members of the Clearing union.

DOLLAR AND THE GLOBAL IMBALANCES

If there is truth in the statement that undervalued of the Chinese value to the American dollar is the reason for the huge foreign trading deficit of USA and the surplus in China, the claiming is far from the overall truth for the reasons of the USA internal deficits and external debt, the weaknesses of dollar and by that for the global imbalances.

It is a fact that the relation of the currencies of the two biggest economies in the world is an important factor which determines the flows of their internal exchange and they largely are expressed onto the international economic relations. But, that is not sufficient argument to make pressing of the rate of Yuan to dollar on the level for necessities for exchange balance of the USA, even more that the value of Yuan to dollar is in a trend of appreciation. It is an argument plus for the necessity to question the justification and the sustainability of the international role of dollars as world money, in conditions of fluctuating exchange rates in the intercurrences relations in the world.

There is no economic reason why the country that has made sufficient appreciation on its own currency[1], constantly press on further appreciation in order to balance the exchange with the largest world economy. The burden of adjustment, by rule, is put on the country which loses the competitive advantages. There should be made corresponding changes in the system and the behavior of the economic subjects which will improve their competitive capability.

The relation between the dollar and Yuan is not the main cause for the imbalanced relations between USA and China nor for the global imbalances,

[1] Chinese currency from June last year to September this year revaluated for 7% and from 2005 for 30% (China daily 2011-10-070). The currency rate of Juan to dollar would really become a problem for which it should be discuses only if the price competition of Chinese export would be achieved with constantly devaluation of the value of Juan to dollar and the other currencies.

and even less for the calls for taking counter measures towards “the currency manipulator” which allegedly, consciously maintenances the undervalued of Yuan to secure competitive advantage of its own products on foreign markets, especially on the market of the United States. It is obvious that even the requested revaluation was achieved of Yuan to dollar, there is still the question if there would be insisted on changes of the Yuan exchange rate if the relations in the exchange would not be improved on the behalf of the USA? How long would requested adjustment of the others last? Where is the market logic to ask by the investment surplus countries to save less and to spend more, to change their development strategies from “export lead growth” to “grown lead by the domestic consumption” (especially in conditions of non consequent international monetary system and under the influence of interests of certain national economy).

Among the reasons for the largest crises after the Second World War and the global imbalances, the USA internal imbalances have their own position. They basically were generated by the policies to satisfy certain social economic necessities of the development (employment, standard of the population in order to alleviate the growing inequalities of the American society) and such policies largely were achieved and with use of the benefits that come out of the international role of dollar as a reserve currency (loans without interests). The key role is in that they had the relaxing monetary policy and the constant growth of the budget and the external trading deficit of the USA.

The relaxing monetary and the loose (unstable) fiscal policy lead to eroding of the purchasing power of dollar.

Table1 Purchasing power of dollar compared to USA dollar from 1980

Year	**Equvalent of purchasing power**
1950	**3.42**
1960	**2.78**
1970	**2.12**
1980	**1.00**
1990	**0.63**
2000	**0.48**
2007	**0.40**
2008	**0.38**

Source: Measuring Worth- Purchasing Power of Money in the United State from 1774 to 2008 (stated according to www.en.wikipedia.org/wiki/ United_ State_dollar)

From the data it can be concluded that in 2008 the dollar was worth only 0, 38 of the dollar's value in 1980.

According to another calculation today's dollar is worth only 0.19 dollars of the dollar in 1971 when its convertibility in gold was abandoned.[2]

These movements direct to the conclusion that USA did not show their affinity to stabilize the value of dollar on foreign markets around fixed parity with margins to limited variations Actually, they left other countries to have the obligation to intervene, if they concluded that it was necessary to preserve the stable relation between the dollar and their currency. If they did not take corresponding measures (adjusted to American interests), for example as China, they were imposed on open pressures and threats.

In meanwhile as Wiggin[3] noted that depreciation of dollar put the planet in disorder and deteriorated the tendencies. The decline of dollar destabilized the economies, created inflation, and impoverished the foreigners that it held as well as the population who lost the purchasing power. By that it can be stated that the dollar is the main risky element in the world of finances[4]

II

The global imbalances are not specificity of modern (actual) international economic relations. They are constantly present in the international economic relations. The problem is that today they are so increased that their overcoming is not possible any more to be achieved with the current measures and activities of the most important actors on the international scene.

The issue of global imbalances existed and it was present even in the system of, but there were rules and if they were respected the imbalances would be overcome. The functioning of the mechanism of gold exchange standard prevented long term generation of external trading surpluses and deficits. Both, surplus and deficit countries were under objective pressure to take measures to balance the relation abroad through actions for maintenance of internal balance. The function of the mechanism of gold exchange standard was eased with the behavior of the monetary authorities. With their own actions they stepped together with the tendencies of the mechanism itself, following "the rules of the game".

Beside following the **postulates for free forging and smelting of golden coins and the free export and import,** the central banks of countries with gold exchange standard not only that interfered the normal functioning of the mechanism of gold exchange standard but were persistent to ease in order to increase its efficiency. For example, at outflow of gold, the Central bank took measures the circuit of money in the country more or less automatically to be reduced. And vice versa in a case of influx of gold their measures went to

---

[2] Stephen Mauzy: Don't Blame the Federal Reserve, Ludwig von Mises Institut, Mises Daily, December 15, 2009.

[3] Addison Wiggin: Le declin du dollar, Publication Agora, 2008, p. 241.

[4] Ibid. p. 206.

that the circuit of money in country to be increased. The disturbed imbalance could be introduced because the monetary authorities respected the rule-influx of gold to be used as a base for increasing and the outflow for reason of reduction of the money circuit. In that direction the central banks acted through the change of the discount rate and through the policy of open market, which is through purchase and selling of bonds.

Theoretically seen, under the regime of international gold exchange standard there was no possibility some country to lose its gold that is to be in fundamental imbalance. There were possible only temporary loses and yields temporary disturbances of the balance of payments which later were corrected with behavior according to the rule of games.

In that context with every right the positive effects from the functioning system of gold exchange standard in the national economies and in the world economy as a whole are attributed to the stability of foreign exchange rates. They were and remain as one of the main preconditions for normal functioning of the world economy. The evolution of metal into paper money systems in the process of dematerialization of money, did not suspend the importance of the stability of inter currency relations in the world. In this context the fluctuating exchange rate used after the breaking down of Bretton Woods system are not as the Nobel Prize winner Mundell stated alternative to the fixed[5]. With their use it was only broaden the list of national currencies, which beside the dollar, will perform a function of world money and was abandoned the natural course in money development as commodity money.

III

Today it can be stated that in Bretton Woods it has been lost the possibility MMS to continue to be based on commodity money (goods as money) considering that in that period there has been made proposal for new MMS by lord J.M Keynes. He suggested creation of world currency –bancor (currency that would be used for trading) with value confirmed in gold but not convertible for gold. But, his proposal was not accepted.

The decision for the new international monetary system Keynes sees in the replacement of the system of gold exchange standard with new accounting

---

[5] Robert Mundell*:* The choice between fixed and flexible exchange rates is an oxymoron. The alternatives are incomparable. A fixed exchange rate system is a monetary rule. A flexible exchange rate is the absence of that particular monetary rule and is consistent with price stability or anything at all, including hyperinflation. The real choice is between a fixed exchange rate monetary rule and alternative monetary rules such as inflation targeting or monetary targeting. The choice between the three monetary rules depends on several factors, including the actual and desired rate of inflation. Assuming a country wants monetary stability, but is in a state of high inflation, it should adopt a monetary rule because the high inflation rate is almost certainly due to excess growth of the reserve base of the money supply (usually fiscal deficits that have to be financed by the central banks). (Robert Mundell and Milton Friedman: One World, One Money?, Policy Options, May 2001).

system based on the mechanism of multiple banking clearing [6].It should enable broadening of international economic exchange, beside the fact that countries do not have sufficient gold and reserves and they would not be in a possibility not even far from payment the export necessities. Such aim should be realized though the International Clearing union where all members of United Nations would be members. The International Clearing Union would be Supreme institution where the balance of the international payments would influx and will be liquidated in a way planned. In the transaction between separate countries- members- the Union is included immediately when some of the countries have no foreign assets.

The key news in the system is creation of separate money- bancors. Their value is expressed in gold (but the value was not confirmed in the plan). The currencies of the countries- members- its value confirm to the bancor. This money is used for leveling of international balances and should be universally accepted as a equivalent for gold. The central banks of the countries members and no members have the right to replenish their Clearing accounts by payment in gold but they can not withdraw gold.

The mechanism of function secures balancing of the exchange without appearance of exaggerated deficits and surpluses. The principle is established of equal liability of the countries debtors and of the countries creditors in the maintenance of balance in the international payments. It is forced each country to accept its own currency to be seen to bancor as international currency and the management with it to accomplish in accord to the discipline that the supranational bank imposes.

When one country appears as debtor to another one, its debt is leveled through the Union in bancors, that is by international credit; the creditors receive bancors and they can use them for international payments (beside that they can not ask gold) they can use it for purchasing of goods, services or to realize it in investments.

How much one country can use of the credit is defined with quotes for each country in amount of 75% of the average range of its external trading for the last three planned years. The overall amount of quotes would be 25 billions dollars. This amount would be 4-5 times greater than the assets which are planned for the functioning of MMF.

Each country is obliged in the limits of 25% of its quite without any special conditions. The increase of the debt above that would be possible with authorization of the Union. If the debt reaches 50% of the quote, the Union can ask to pass a guarantee (in gold, domestic currency, state's securities). In this context, the quotes, that is credits have expansive but also contraction role in external commerce. They enable goods to be supplied abroad even when there no means but the excessive debt is stopped. By that the balance in the international payments is preserved.

---

[6] J.M. Keynes: Proposals for an International Currency Union (Second Draft, November 18,1941)

From the several rules important for the function of the Clearing system (with the creation of bancor) that is proposed by Keynes, it is clear that it remains on line of commodity money. He just reduces the use of gold (to avoid the race for “barbaric relic”) but, remains in changed circumstances to preserve some of the essential rules for the functioning of the gold exchange standard. Proposing bancors (world credit money), he stands for the stability of foreign exchange rates in intercurrence relations in the world, for balancing of international economic relations, that is for securing conditions each country to enjoy the fruits of its (un)success.

There is no doubt that such aims could be achieved with the foundation of the International Clearing Union which will have the right to issue bancors in amount which will satisfy the objective necessities (market verified) on the international turnover. It is clear that in such transactions will appear countries with deficit and with surplus. But, not to separate permanently surplus and permanently deficit countries, he proposes the countries which make surplus above certain limit to pay certain compensation presuming that they preserve undervalued currency and the countries which make deficit on that base to pay certain compensation presuming that they preserve appreciated national currency. He allows corrections of the exchange rates in order to overcome the balances of the fundamental imbalances and by that to make balance in the international economic relations.

In that context it can be said that today’s world survived the consequences from the **abandoning of the evolution of money** as commodity money in the international economic relations and in function of world money appeared dollar and latter DM, jean and the Euro. The consequences can be systematized in the statement that the dollar is national currency but the problems of dollar are worldwide, while in the concept of Keynes world money is created and the problems of the national currencies are problem of the national economies. This is surely basis for overcoming of the global imbalances or at least for their equalizing on level to be successfully managed by advance confirmed rules.

Conclusion

In the overcoming of global imbalances it must be started from the reasons which generate imbalances for a longer period. At the same time, it should not be bypassed the dollar's role as a world currency.

For the exiting global imbalances there is no permanent solution without deep reform of the international monetary system, because the actual imbalance is consequence of the function of the no consistent international monetary order.

The global imbalances can not be solved without approaching simultaneously from one side to leveling of the deficits on sustainable level and from the other side to substitution of the international role of dollar (with consideration of that it is the alibi of "construction" of deficit in the current balance of USA).

Only with the function of world currency (opposite to the function of the national currencies as world money) it can be considered that it will enable to overcome the situation where the national economic problems will be manifested as world, which largely burden the international economic and political relations.

Bibliography

1. Claudio Borio and Piti Disyatal : Global imbalances and the financial crisis: Link or no link? Bank for International Settlements,, Working papers, No. 346, May 2011.
2. J.M. Keynes: Proposals for an International Currency Union (Second Draft, November 18,1941)
3. Bernard SCHMITT: New Proposals for world monetary reform, 1973, Castella
4. Edwin M. Truman: The International Monetary System and Global Imbalances, Petrson Institute for International Economics, January 2010.
5. Dr. Robert A. Mundell: Exchange Rates, Currency Areas and the International Financial Architecture- www.usagold.com/gildedopinion.
6. Robert Skidelsky: Keynes, Globalisation and the Bretton Woods Institutions in the Light of Changing Ideas about Markets, World Economics, Vol.6, No.1, 2005).
7. Kenneth Rogoff: Global Imbalances without Tears, Project Syndicate, 2001-03-01.
8. Paul Krugman: World Out of Balance, The New York Times, November 16, 2009
9. Joseph E. Stiglitz: Death Cometh for the Greenback, The National Interest on line, November/December 2009.