

The Global Economic Crisis:

Systemic Failures and
Multilateral Remedies



UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT

The Global Economic Crisis: Systemic Failures and Multilateral Remedies

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Systemic Issues and Economic Cooperation



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Key messages

UNCTAD's longstanding call for stronger international monetary and financial governance rings true in today's crisis, which is global and systemic in nature. The crisis dynamics reflect failures in national and international financial deregulation, persistent global imbalances, absence of an international monetary system and deep inconsistencies among global trading, financial and monetary policies.

National and multilateral remedies

- **Market fundamentalist *laissez-faire* of the last 20 years has dramatically failed the test. Financial deregulation created the build-up of huge risky positions whose unwinding has pushed the global economy into a debt deflation that can only be countered by government debt inflation:**
 - *The most important task is to break the spiral of falling asset prices and falling demand and to revive the financial sector's ability to provide credit for productive investment, to stimulate economic growth and to avoid deflation of prices. The key objective of regulatory reform has to be the systematic weeding out of financial sophistication with no social return.*
- **Blind faith in the efficiency of deregulated financial markets and the absence of a cooperative financial and monetary system created an illusion of risk-free profits and licensed profligacy through speculative finance in many areas:**
 - *This systemic failure can only be remedied through comprehensive reform and re-regulation with a vigorous role by Governments working in unison. Contrary to traditional views, Governments are well positioned to judge price movements in those markets that are driven by financial speculation and should not hesitate to intervene whenever major disequilibria loom.*
- **The growing role and weight of large-scale financial investors on commodities futures markets have affected commodity prices and their volatility. Speculative bubbles have emerged for some commodities during the boom and have burst after the sub-prime shock:**
 - *Regulators need access to more comprehensive trading data in order to be able to understand what is moving prices and intervene if certain trades look problematic, while key loopholes in regulation need to be closed to ensure that positions on currently unregulated over-the-counter markets do not lead to "excessive speculation".*
- **The absence of a cooperative international system to manage exchange rate fluctuations has facilitated rampant currency speculation and increased the global imbalances. As in Asia 10 years ago, currency speculation and currency crisis has brought a number of countries to the verge of default and dramatically fuelled the crisis:**
 - *Developing countries should not be subject to a "crisis rating" by the same financial markets which have created their trouble. Multilateral or even global exchange rate arrangements are urgently needed to maintain global stability, to avoid the collapse of the international trading system and to pre-empt pro-cyclical policies by crisis-stricken countries.*

Global economic decision-making

- **The crisis has made it all too clear that globalization of trade and finance calls for global cooperation and global regulation. But resolving this crisis and avoiding its recurrence has implications beyond the realm of banking and financial regulation, going to the heart of the question of how to revive and extend multilateralism in a globalizing world.**
- **The United Nations must play a central role in guiding this reform process. It is the only institution which has the universality of membership and credibility to ensure the legitimacy and viability of a reformed governance system. It has proven capacity to provide impartial analysis and pragmatic policy recommendations in this area.**

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Abbreviations

BIS	Bank for International Settlements
CBOT	Chicago Board of Trade
CDO	collateralized debt obligations
CDS	Credit Default Swaps
CEA	Commodity Exchange Act
CEBS	Committee of European Banking Supervisors
CESR	Committee of European Securities Regulators
CITs	commodity index traders
CFTC	Commodity Futures Trading Commission
COT	Commitments of Traders
DJ-AIGCI	Dow Jones-American International Group Commodity Index
ECB	European Central Bank
FED	Federal Reserve System
FSA	Financial Services Authority
GDP	gross domestic product
ICE	Intercontinental Exchange
IMF	International Monetary Fund
LTCM	Long-term Capital Management
OTC	over-the-counter
NEER	nominal effective exchange rate
PEER	price component of REER (PEER=NEER/REER)
PPP	purchasing power parity
REER	real effective exchange rate
RMBS	residential mortgage-backed securities
SIVs	Structured Investment Vehicles
S&P GSCI	Standard & Poor's Goldman Sachs Commodity Index

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