T.C
İNÖNÜ ÜNİVERSİTESİ
İKTİSADİ VE İDARİ BİLİMLER FAKÜLTESİ

TURGUT ÖZAL ULUSLARARASI EKONOMİ VE SİYASET KONGRESİ-1
KÜRESEL KRİZLER VE EKONOMİK YÖNETİŞİM
BİLDİRİLER KİTABI

TURGUT OZAL INTERNATIONAL CONFERENCE ON ECONOMICS AND POLITICS-1
GLOBAL CRISES AND ECONOMICS GOVERNANCE
CONFERENCE BOOK

EDİTÖRLER

Doç. Dr. Ali KOÇYİĞİT
Doç. Dr. Levent GÖKDEMİR
Doç. Dr. Hakan ERKUŞ
Yrd. Doç. Dr. Recep KARABULUT
Yrd. Doç. Dr. Selahattin BAKAN
Yrd. Doç. Dr. Suzan ERGÜN

15-16 Nisan 2010 MALATYA

ISBN 978-975-8573-08-0

Yayına Hazırlama ve Dizgi
Araş. Gör. Selim DEMEZ İbrahim DİKER

Nisan 2010
İnönü Üniversitesi
İktisadi ve İdari Bilimler Fakültesi
İnönü Üniversitesi Yerleşkesi
Elazığ Yolu 12. Km 44280 Malatya
Tel: (422) 341 00 43
http://ozal.congress.inonu.edu.tr

TÜRKİYE
FİNANS

Bu Kitap Türkiye Finans Katılım Bankası Katkıları ile Yayınlanmıştır.

Düzenleme Kurulu

Onursal Başkan: Prof. Dr. Cemil ÇELİK (Rektör)

Kongre Başkanı: Prof. Dr. Çetin DOĞAN

Doç. Dr. Ali KOÇYİĞİT

Doç. Dr. Fikret OTLU

Yrd. Doç. Dr. Nihat AKBIYIK

Yrd. Doç. Dr. Selahattin BAKAN

Yrd. Doç. Dr. Sait PATIR

Yrd. Doç. Dr. A. Fahimi AYDIN

CRISES AND NEW INTERNATIONAL POLICY

Shafag Mammadova [1], Orhan Cheltikchi[2]

Abstract

The industrialized world has been undergoing a recession, a pronounced deceleration of economic activity in the United States in December 2007. There was optimistic air in world markets before the crises. The oil price rose, the drought was one of the factors that made crucial impact on the crises, and price in food products also rose and it overturned to crises. A global recession has resulted in a sharp drop in international trade, rising unemployment and slumping commodity prices.

The crisis affected financial area high and it created deep influence in world markets. In order to show the terrible results of the crises it is compared with the crisis happened in 1929. That times crises impact the USA and increased unemployment.

The crisis affected all countries in some ways, but certain countries vastly affected more than others. It affected countries policy and the crises drew the new world policy.

What are the factors of World Economic Crises? What was the impact of the WEC to the states policy? , How to overcome the crises? These questions will be clarified in our article.

Keywords: recession, self-insurance, off balance-sheet, stimulation, fiscal

[1] MA.Shafag Mammadova, Department of International Relations, Azerbaijan University of Languages, Baku. Sebail, Azerbaijan, email: shafag_mc@yahoo.com, Tel: (+994) 050 5644468, Fax: (+994) 0124655957

[2] PhD,Orhan Cheltikchi, Department of History, Akdeniz University, Antalya, Turkey, email: umaykaan250@hotmail.com, Tel: (+90) 5399815465, Fax: (+90) 5058586100 www.orhanceltikci.com

1. The Financial Crisis

Humanity as a whole possesses enormous resources in the form of financial means, technological know-how, manpower, and womanpower. Modern science has developed effective means that could solve most of the urgent problems in today's world – combat the majority of diseases, eliminate hunger and poverty, reduce the amount of industrial waste, and replace destructive fossil fuels by renewable sources of clean energy. The problems that stand in the way are not of an economical or technological nature; their deepest sources lie inside the human personality.

Because of them, unimaginable resources have been wasted in the absurdity of the arms race, power struggles, and the pursuit of "unlimited growth." They also prevent a more appropriate distribution of wealth among individuals and nations, as well as a reorientation from purely economic and political concerns to ecological priorities that are critical for survival of life on this planet. (Miller Calum, 2005; 4)

Diplomatic negotiations, administrative and legal measures, economic and social sanctions, military interventions, and other similar efforts have had very little success. It is becoming increasingly clear why they had to fail. The strategies used to alleviate this crisis are rooted in the same ideology that created it in the first place. In the last analysis, the current global crisis is basically a psycho spiritual crisis; it reflects the level of consciousness evolution of the human species. It is, therefore, hard to imagine that it could be resolved without a radical inner transformation of humanity on a large scale and its rise to a higher level of emotional maturity and spiritual awareness.

The task of imbuing humanity with an entirely different set of values and goals might appear too unrealistic and utopian to offer any real hope. Considering the paramount role of violence and greed in human history, the possibility of transforming modern humanity into a species of individuals capable of peaceful coexistence with their fellow men and women regardless of race, color, and religious or political conviction, let alone with other species, certainly does not seem very plausible. We are facing the necessity to instill humanity with profound ethical values, sensitivity to the needs of others, acceptance of voluntary simplicity, and a sharp awareness of ecological imperatives. At first glance, such a task appears too fantastic even for a science-fiction movie.

However, although serious and critical, the situation might not be as hopeless as it appears. After more than half a century of intensive study of holotropic states of consciousness, I have come to the conclusion that the theoretical concepts and practical approaches developed by transpersonal psychology, a discipline that is trying to integrate spirituality with the new paradigm emerging in Western science, could help alleviate the crisis we are all facing. These observations suggest that radical psycho spiritual transformation of humanity is not only possible, but is already underway. The question is only whether it can be sufficiently fast and extensive to reverse the current self-destructive trend of modern humanity.

The global financial system is in crisis the global financial crisis, the most severe since the Great Depression, is rapidly turning into a human and development crisis. The financial crisis originated in the developed world, but it has spread quickly and inexorably to the developing world, sparing no country. Increasingly it appears that this will not be a short- lived crisis. The poor countries are especially vulnerable, as they lack the resources to respond with ameliorative actions. The crisis poses serious threats to their hard-won gains in boosting economic growth and achieving progress toward the Millennium Development Goals (MDGs). Poor people typically are the hardest hit, and have the least cushion. For millions of them, the crisis puts at risk their very survival. (Williem, 2008; 3-4)

For poor countries, this is a crisis upon crisis. It comes on the heels of the food and fuel crises. The triple jeopardy of the food, fuel, and financial crises is pushing many poor countries into a danger zone. Those that opened their doors to global finance have seen huge increases in their vulnerability to shocks like the one we are living through now, but little more in the way of improved human development than countries which took a more cautious approach. And the poorest countries have not got the financing they so desperately need. It is becoming increasingly clear that we need a system that actually serves development without the huge risks that are now all too apparent.

With the seizing-up of the international financial markets in 2008, emerging market countries were the first among developing countries to feel the impact of the financial crisis, given their heavier reliance on private capital flows.

Many low- income countries are also affected. The impact of the global financial crisis on developing countries is reflected in sharp reductions in their projected GDP growth to rates that are the lowest since the 1990s.

Although developing countries didn't make this crisis, it has become all too clear that they are in the firing line when it comes to suffering its effects. Many descriptions of the current financial crisis have drawn on the metaphor of natural disaster. Storms, earthquakes and floods have all been invoked to describe the scale and destructive power of the financial forces that have been unleashed. But while this gets across the impact of what has happened, it is totally misleading in one respect. The financial crisis is not a natural disaster – it was made by people, and is the product of decisions made by companies and by governments – decisions that could have been made differently, and could have led to very different outcomes. The crisis is actually two crises – a financial crisis and a recession.

2. Crisis Impact on States

What determines how different countries are likely to be affected? In this article we look at the very different ways that countries have integrated into the global economy, and how this leads to very different outcomes in the current upheaval. One thing we haven't known until now is exactly how the shockwaves from the crisis have travelled around the world, and how big those shocks are going to be. We've had stories of job losses, and the threat of reductions in aid flows, but no systematic look at what this means for the poorest and most vulnerable people on earth.

The expansion of 2002-07 began with a bang – the bursting of the US tech-stock bubble in 2000-01, which had a substantial wealth effect on American households. To minimize the duration and depth of the ensuing recession, the Federal Reserve aggressively eased monetary policy. It lowered either the Fed funds rate or the discount rate 27 times between January 2001 and June

2003. This expansionary monetary policy averted a deeper recession by stimulating a boom in the housing market, which soon turned into a housing bubble. Because of the large share of the housing stock in household wealth, this bubble overcompensated greatly for the loss of wealth in the stock market decline of 2000-02. Higher housing prices fueled a consumption boom, and the Fed's continued expansionary monetary policy kept the US economy awash in excess liquidity. Another essential ingredient behind the persistently low US (and global) real interest rates was the shift of developing countries toward accumulating large volumes of US assets, motivated by their experience in previous crises and made possible by their current account surpluses. This made it possible for the US to finance its massive current account deficit over a prolonged period without abrupt changes in real interest rates or real exchange rates. (Alesina, Alberto and Drazen, 1991; 88) The financial crisis has already led to catastrophic drops in income in 2008, 2009. A large number of developing countries and the economies in transition have been reluctant to ease monetary policy over concerns of inflationary pressures and currency depreciation. Inflationary pressures should taper off during 2009, however, as world food and energy prices are now retreating and global demand is weakening. This should provide some space for monetary easing, as well as for fiscal stimulus, at least in those countries that still possess ample foreign-exchange reserves. The scope for counter-cyclical policies will vary greatly across developing countries, mainly for two reasons. First, many countries have a history of pro-cyclical macroeconomic policy adjustment, partly driven by policy rules (such as inflation targeting). Providing greater monetary and fiscal stimuli in such cases will thus require a departure from existing policy practice and policy rules. Second, not all countries have equally sufficient foreign exchange reserves and some are likely to suffer stronger balance-of-payments shocks. There are countries with ample policy space for acting more aggressively to stave off a recession. The Chinese Government has already started to use its policy space, for instance, and has designed a large-scale plan of fiscal stimulus amounting to 15 percent of its GDP to be spent during 2009 and 2010, which should contribute to reinvigorating global demand. The Republic of Korea has also announced a fiscal stimulus package equivalent to 1 per cent of its GDP.

Considering that the pre-crisis forecast was that earning from trade and private sector flows should actually rise between 2007 and 2009, the crisis has clearly hit hard and hit quickly. The financial crisis will affect factors such as bank lending, equities and foreign direct investment, and changes in interest rates will impact on countries and companies that raise money by issuing bonds. For countries that based all or part of their development strategies on attracting funds from abroad, and for the companies and individuals that were dependent on these flows, this fall is likely to be calamitous. However, for many countries their openness to and dependence on private sector flows such as private bank lending from abroad has increased – in many cases dramatically. As the financial bubble grew in developed countries, developing countries were becoming increasingly vulnerable to the bursting of that bubble. According to the IMF, the impact of financial crises is likely to be more serious, and more long-term, than the impact of recessions that have other causes, such as cyclical slowdowns in the economy. In increasing their vulnerability to financial crises, developing countries have therefore increased their risks of exposure to these more serious recessions.

Devising indices and typologies to show which countries are likely to be most vulnerable to the financial crisis and the recession has become a popular pastime in development circles. One of the World Bank's two typologies looks only at poverty measures and at the fiscal and institutional aspects of the government's ability to cope. It does not address how countries' exposure to the crisis might differ given different levels of dependence on international trade or finance. The second World Bank typology contains both trade and finance variables, but it still does not reflect how countries are likely to experience vulnerability in the real world. For example, trade vulnerability is only measured according to whether or not a given country is dependent on primary commodity exports. While important to one group of countries, this misses out the huge impact of the fall in demand for manufactured products, which is having such devastating effects throughout Asia. (Akyuz, 2008; 7)

The impact of policy on vulnerability to both financial crisis and recession is starkly illustrated in the differing fortunes of South Africa, India, China and Brazil. All members of the G20, different policy choices in the 1990s and early 21st century mean that the crisis will have a very different impact on each of these four countries. The crucial difference lies in how countries are integrated into the global economy. China and India have historically been less open to the global economy than many other developing countries, and both have retained capital controls. Brazil is more open and South Africa more open still.

In China the majority of growth to date has been based on expanding exports, which means that the recession is already hitting hard. However the financial crisis is likely to have less impact, since the government has restricted flows of foreign capital and most Chinese investment and other finance comes from within the country. While its financial system is relatively closed, China is the most dependent on external trade of all four countries.

The immediate threat in China is real. A large part of China's economic success over the last 10 years has been based on a strategy of export-led growth. The financial crisis shows that this was a risky strategy – but it is one that has been key to providing jobs for millions of migrants moving to the cities from urban areas, and has brought China many billions of dollars of export revenue over the years.

1. **<u>Developed economies</u>**

Among developed economies, the economy of the United States is expected to decline by 1 percent in the baseline scenario for 2009. The most severe credit crunch since the Great Depression has turned a housing sector-led slowdown into a full-scale retrenchment of households and businesses, affecting the economy at large. Even though effective implementation of the Emergency Economic Stabilization Act (EESA), together with other measures, may eventually stabilize financial markets, it came too late to prevent a recession in the real economy. The unemployment rate is expected to rise above 7 per cent as job losses in almost all sectors of the economy increase sharply. Inflation, by contrast, is expected to abate notably. Should all the policy measures fail to unclog the credit markets soon, the United States most probably will suffer a much deeper and longer recession. Japan's economy is in a recession and is expected, at best, to stagnate in 2009. While the direct losses from the global financial crisis have been contained so far, the indirect effects are becoming increasingly significant, including those brought on by weakening external demand as well as the appreciation of the yen. Since September 2008, the global credit crunch has transformed a sharp slowdown in Western

Europe into a full fledged recession, and the major European economies have technically entered into recession. Having lost all growth momentum, GDP is expected to contract further in the first half of 2009, with little likelihood of recovery in the second half, leaving a negative growth rate for the year as a whole. After a long period of improving labour market conditions, unemployment rates began to drift upwards from mid-2008 and are expected to move up further by nearly a full percentage point on average for the region as a whole in 2009. With activity slowing, and commodity prices falling well below their peaks of mid-2008, inflation is expected to decelerate significantly from the highs experienced during 2008. Risks continue to be slanted towards the downside, particularly as regards the effectiveness of current and anticipated policies in stabilizing financial markets. Following several years of buoyant economic expansion throughout the entire region, the new EU member States exhibited divergent growth patterns in 2008. Domestic demand is weakening in response to higher credit costs and accelerated inflation, and export growth is also likely to decline. Growth is expected to weaken and inflation to moderate in 2009. While the new EU members are not directly exposed to the sub-prime loans of the United States, the region's banking system is subject to the shocks generated by the troubles among financial institutions in the EU-15. The high stock of short-term private debt in foreign currencies has already created a serious liquidity squeeze in Hungary. The risks for the region include a protracted slowdown in the EU-15, as well as a sharp reversal of capital flows.(www.voxeu.org, Szekely, Noord, 2009) In other developed economies, growth in both Australia and New Zealand are slowing as consumer demand has weakened owing to tighter credit conditions, higher inflation and falling asset prices. The Canadian economy will suffer from the economic slowdown in the United States, especially in sectors such as the automotive industry.

2. Economies in transition

Among the economies in transition, growth of the members of the Commonwealth of Independent States (CIS) is heading for a marked slowdown in 2009, largely dragged by the impact of the global recession and falling commodity prices on the largest economies, such as Kazakhstan, the Russian Federation and Ukraine. A slowdown in business investment, and, to a lesser degree, in household consumption will be felt throughout the region. The smaller CIS economies will likely be affected by declining worker remittances and FDI inflows. The adverse effects of a domestic credit squeeze and increased costs of external financing will be significant on the real economy of the region, despite some recently adopted offsetting policy measures. The unemployment rate will increase in some countries, while inflation is set to moderate, although it could remain at elevated levels. Among the downside risks, a worse-than-expected growth in the Russian Federation would have recessionary effects on other members. In South-eastern Europe, growth in 2008 continued to be largely driven by domestic demand, underpinned by rising real wages and the lasting credit boom, as well as by strong FDI inflows. (Triquell, 2009; 2) With the global financial crisis, these growth factors have started to lose momentum. In view of the weak demand in their main export markets, it is also unlikely that the region would be able to switch to a more export-oriented pattern of economic growth in the short run. Therefore, a further moderation of economic growth is expected in 2009. (Vos, Hong, 2009; VII)

3. Developing countries

Developing countries will be hurt by the crisis through international trade and finance channels. The drop in commodity prices will hurt primary exporters in particular, but lower demand in the developed countries will affect export growth throughout the developing world. Some emerging market economies, such as Brazil, are already facing severe curtailments in access to trade credit, while the threat of a sudden reversal in private capital flows has heightened. (Lin Senior, 2008; 5-6) The vast amounts of foreign reserves accumulated by developing countries still provide a buffer and allow some space for counter-cyclical measures, but these reserves could well dwindle rapidly as the global crisis deepens further. A growing number of developing countries have already witnessed a significant deceleration in economic growth. This, no doubt, is diminishing the prospects of achieving the Millennium Development Goals (MDGs).Growth in Africa is expected to decelerate to 4.1 per cent in 2009 from 5.1 per cent in 2008, as the contagion effects of the global economic slowdown spread throughout the region, while inflationary pressures continue to dampen consumer demand. Africa would be impacted through weakened export demand, lower commodity prices and a decline in investment flows to the region. Consequently, employment growth in Africa is anticipated to weaken, pushing unemployment rates higher and forcing more workers into the already large informal economy. Inflation is expected to subside from 2008 levels. Risks for greater growth retardation exist if donor countries do not live up to their aid commitments, threatening not only the achievement of the MDGs, but also undermining past progress. Growth in East Asia is expected to decline notably in 2009, as exports will decelerate significantly. Some economies in the region will also experience sizeable financial losses as a result of their relatively high exposure to global financial markets. An outflow of capital from this region will further intensify the difficulties experienced by the local financial institutions. Inflation in the region is expected to moderate, and the employment situation will start to deteriorate. Further monetary easing is expected in the region, and most countries have enough policy space to adopt more expansionary fiscal policy necessary for stimulating domestic demand. Some countries, such as China and the Republic of Korea, have already taken action in that direction. South Asia is experiencing an overall slowdown in economic growth from the industrial sector to the service sector as a result of the negative impact of higher costs and the global financial turmoil. Inflation is forecast to moderate in view of the retreat in energy and food prices, resulting in lower pressure on government budgets related to price subsidies. During 2008, external balances suffered from higher import prices for fuel oil, food and other commodities, although continued solid remittances exerted a certain stabilizing effect in this regard. The financial sector in the region has had only very limited direct exposure to the global financial crisis, but the tightening in liquidity emerged as a major indirect impact. In parallel to this, waning investor confidence has led to capital outflows and shrinking foreign-exchange reserves. A number of downside risks include a more prolonged slowdown in global growth, unsustainable fiscal balances and current accounts, natural disasters and political instability. Pakistan is a case in point where all of these factors have already come to a head. Growth in Western Asia is anticipated to slow down significantly in 2009, to the lowest rate in seven years. The region will register a sharp decline in export revenues as average annual oil prices are expected to drop. Lower oil revenues and deteriorating credit conditions in the countries of the Gulf Cooperation Council (GCC) are likely to trigger a delay of large investment projects throughout the region. Facing large current account deficits, the economies of Jordan, Lebanon and, in particular, Turkey appear to be the most vulnerable to a drop in FDI inflows and tighter financing conditions. By contrast, strong fiscal and external positions will allow authorities in GCC countries to maintain an expansionary fiscal policy stance in order to weather the economic downturn. While labour markets have already started to deteriorate in a number of countries, most pronouncedly in Turkey, the high inflation rates throughout the region are expected to decline moderately. Economic growth in Latin America and the Caribbean is expected to slow markedly in 2009. (Green, 2009; 5) The key drag is the fall in commodity prices. In addition, domestic credit is expected to tighten in many economies. Inflationary pressures, which surged during 2008 owing to the increasing costs of energy, transportation and food, should decelerate in 2009, but Governments of the region may not be able to ease monetary policy in the face of currency depreciation. Stimulus will have to come through counter-cyclical fiscal policies, for which most countries have some room to man oeuvre given improvements in external and fiscal positions in preceding years. However, the region remains very vulnerable to an intensification of the global credit crunch, particularly a sharper reversal of capital inflows and a further decline of external demand.

Policymakers initially responded in piecemeal fashion, failing to see the systemic risk or to consider the global ramifications of the turmoil in their entirety. As the crisis intensified in September 2008, policymakers shifted to a more comprehensive and internationally improved coordinated form of crisis management. The measures taken have reshaped the previously deregulated financial landscape. Massive public funding has been made available to recapitalize banks, taking partial or full ownership of failed financial institutions and providing blanket government guarantees on bank deposits and other financial assets.

Governments in both developed and developing countries have started to put together fiscal and monetary stimulus packages in attempts to prevent the global financial crisis from turning into a worldwide human disaster.

Looking to the long run, however, a broadening of the development policy framework is needed to conduct active investment and technology policies so as to diversify these countries' economies and reduce their dependence on a few commodity exports, thereby allowing them to meet key development goals, including reaching greater food security, addressing climate change and meeting the Millennium Development Goals. This will require massive resources for public investment in infrastructure, food production, education and health, and renewable energy sources. The crisis also presents various opportunities to align fiscal stimulus packages with long-term goals for sustainable development. The risk of a hard landing of the United States dollar is intrinsic to the very nature of the global reserve system, which uses the national currency of the United States as the main reserve currency and instrument for international payments. Under this system, the only way for the rest of the world to accumulate dollar assets and reserves is for the United States to run an external deficit. However, as the net liability position of the United States continues to increase, investors will start anticipating a readjustment and confidence in the dollar will erode.

Over the past decade, many developing countries have accumulated vast amounts of foreign-currency reserves, providing some "self-insurance" against external shocks. However, both the carry cost of holding such reserves and the opportunity costs of not using them for long-term investment purposes are high. The tendency to accumulate a large amount of reserves in developing countries has its roots in more fundamental deficiencies of the international monetary and reserve system. Improved macroprudential capital-account regulation can help reduce the need for the cost of self-insurance via reserve accumulation. The need for self-insurance can be reduced further with more effective mechanisms for liquidity provisioning and reserve management at the international level, both regionally and multilaterally. More generally, all IMF facilities should be significantly simplified and include more automatic and quicker disbursements proportionate to the scale of the external shock. Recent action has been undertaken in this direction with the reform of the IMF Exogenous Shocks Facility. But total resources remain limited and much more is needed to provide collective safeguards for large-scale crises

3. The Ways to Overcome the Financial Crisis

1. <u>A pessimistic scenario</u>

Given the great uncertainties with regard to how deep this financial crisis could become and how effective the policy measures in place would be, risks for the world economy to perform even worse than in the already gloomy baseline outlook remain high. The key factor in a more pessimistic scenario of this kind would be a much sharper-than-anticipated decline in net lending to households and businesses in major developed countries, not unlike the experience of the United Kingdom of Great Britain and Northern Ireland, Japan and the Scandinavian countries during their respective financial crises in the early 1990s. The lack of confidence and trust in the financial sector would be prolonged, especially if, for instance, large "off balance-sheet" positions of financial institutions continued to disguise risks at much larger financial losses. As a result, the fire sale in equity markets and drops in asset prices will also be prolonged, along with deteriorating indicators of the real economy, including falling business profits and rising unemployment. As financial institutions continue to deleverage and investors become even more risk averse, the pessimistic scenario assumes an extended vicious circle of asset price deflation and perceptions of rising financial risk. The wealth losses from a further sell-off in assets worldwide could completely dwarf the attempts at recapitalization of financial institutions and corporate businesses put in place by the Governments of major developed countries, and make the financial rescue look seemingly impossible. This will erode market confidence further. Developing economies would be hurt more through a deeper recession in the developed economies, a steeper fall in commodity prices and a sharper reversal of capital inflows. Aid budgets could come under greater pressure and affect low-income countries relying on official development assistance not only for their long-term development but also as a cushion against external shocks.

In this scenario, fiscal and monetary stimulus is likely to be less effective. First, it could push the United States and parts of Europe into a "liquidity trap"—akin to that of Japan during the 1990s—where monetary easing would fail to stimulate private consumption and investment. Second, the deep risk aversion and lack of confidence force banks to use any liquidity injections to shore up their balance sheets without enhancing the credit supply to households and businesses. Third, fiscal stimulus also fails to restore confidence among market agents as they fear that Governments lack sufficient means to finance ever-larger bailouts of the financial system or that exorbitant increases in public debt will be a threat to economic stability in the future.

2. An optimistic scenario

In contrast, in a more optimistic scenario, it is assumed that financial market confidence is restored as quickly as assumed in the baseline.

3. The way forward

Given the existing systemic flaws, it seems paramount that deliberations on a new international financial architectures should address at least four core areas of reform:

(a) The establishment of a credible and effective mechanism for international policy coordination. To guide amore inclusive process, the participation not only of major developing countries but also of more representative institutions of global governance is required; hence, a fundamental revision of the governance structure and functions of the IMF and the World Bank is needed.

(b) Fundamental reforms of existing systems of financial regulation and supervision to prevent the re-emergence of excesses.

(c) Reform of the present international reserve system, away from the almost exclusive reliance on the United States dollar and towards a multilaterally backed multi-currency system which, perhaps, over time could evolve into a single, world currency-backed system.

(d) Reforms of liquidity provisioning and compensatory financing mechanisms backed through, among other things, better multilateral and regional pooling of national foreign-exchange reserves and avoiding the onerous policy conditionality attached to existing mechanisms.

The crisis is global; hence, global solutions are needed

World leaders have acknowledged these needs for reform. At the Follow-up International Conference on Financing for Development to Review the Implementation of the Monterrey Consensus, held in Doha, Qatar, from 29 November to 2 December 2008, Governments agreed to address systemic problems and fundamentally reform the global financial system.

At the Conference, donors also promised to honour all commitments to bridge existing deficiencies in official development assistance to developing countries and emphasized that the financial crisis should not stand in the way of achieving this. The global financial crisis could motivate countries to recur to greater trade protection. At the Doha conference on financing for development, Governments pledged to resist such temptation, but also stressed the need to break the impasse in the negotiations to complete the Doha Round of multilateral trade negotiations and safeguard its development dimensions, in particular the principle of special and differential treatment. It will not be easy to find consensus among all stakeholders on the precise shape of a new system of global economic governance, but the risk of endangering global peace and prosperity by failing to address the systemic problems underlying the present crisis are simply too high. This awareness should be the common ground for seeking common solutions.

References

ALESINA, ALBERTO AND ALLAN DRAZEN (1991). Why Are Stabilizations Delayed?" American Economic Review

DIRK WILLEM (2008). "The global financial crisis and developing countries". Overseas Development Institute.

DUNCAN GREEN, OXFAM GB, (2009) "Latin America and the Global Economic Crisis".

JULI MINOVES- TRIQUELL (2009) "The World Economic Crisis". Liberal International

MILLER CALCUM. (2005) "The Human Development Impact of Economic Crises" Human Development Report. Report office official paper.

ROB VOS, PINGFAN HONG, (2009) "A synchronized global downturn" World Economic Situation and Prospects. United Nations

YIFU LIN SENIOR (2008) "The Impact of the Financial Crisis on Developing Countries" The World Bank Korea Development Institute, Seoul October 31,

YILMAZ AKYUZ (2008) "The Global Financial Turmoil and Asian Developing Countries" Briefing Paper 47..

http://www.voxeu.org/index.php?q=node/4065 ISTVÁN P. SZÉKELY, PAUL van den NOORD, (I 6 October 2009) "Economic crisis in Europe: Cause, consequences, and responses". A report by the European Commission,