INTERNATIONAL FINANCIAL CRISIS, G-20 AND GLOBAL POLICY RESPONSE

MEĐUNARODNA FINANSIJSKA KRIZA, G-20 I GLOBALNI ODGOVOR EKONOMSKE POLITIKE

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Abstract: *Gauged against despair of global recession just weeks before the G-20 gathering, the London summit appeared a spectacular, historically unifying and «full-figured» success in modern international finance. However, this paper strives to take a closer look at the backstage nature and true measurements of the announced reforms as well as beef-up funds earmarked in the G-20's London communiqué. Through the process of differentiating between finally achieved and -God-willing- yet to be arranged treatment of the global financial crisis, article exposes arguably remarkable superficiality of the IFIs' reform thus far, in both financial and essential sense. On the other hand, global(ised) economy, more than ever before, is crying out for globally coordinated management&regulation. Even though it became evident that policy measures which mitigated -what now seems as slowly dissipating- financial crisis and worldwide recession were at least 70 years old economics, having next to nothing worth reaping from recent financial crises literature or indeed (re)actions of multilateral financial guardians, still neither full recovery nor regaining control over globalisation could dawn without reform of international financial architecture. Hence, a fundamentally upgraded economic trigonometry among the IMF, (followed by the largely neglected) World Bank and BIS is put forward as a hopefully more able and further reaching proposal for policy oriented responsibility sharing. In concluding remarks, once again, an attempt has been made to depart from the normative analysis in order to sketch the likely outcomes for the crisis-struck global economy, with particular emphasis on critical lessons in retrospect as well as the couple of caveats ahead.*
Key Words: *international financial crisis, London summit, G-20, quota reform, ILOLR, tax heavens, protectionism, SDR creation, Bretton-Woods 2.0, the IMF stigma, the purpose of the BIS , the World Bank's repositioning, global policy response, the world economy, caveats ahead.*

Sažetak: *U poređenju sa očajem pred globalnom recesijom od pre samo par nedelja uoči skupa G-20, Londonski samit se doima spektakularnim, istorijski ujedinjujućim i «cifarski krupnim» uspehom u modernim međunarodnim finansijama. Međutim, ovaj papir pobliže osmatra zakulisnu prirodu i prave razmere kako najavljenih reformi tako i finansijke podrške zacrtane Londonskim memorandumom. Kroz proces identifikacije najzad učinjenog i onoga što –uz božju pomoć- tek treba uraditi na saniranju globalne finansijske krize, članak rasvetljava zapravo neverovatnu površnost u reformi međunarodih finansijskih institucija do sada i to i u finansijskom i u suštinskom smislu. Nasuprot tome, globalizovana svetska privreda, više nego ikada ranije, vapi za globalno koordiniranim upravljanjem i regulacijom. Iako je postalo jasno da su preduzete mere ekonomske politike koje su zauzdale –danas čini se polako jenjavajuću- finansijsku krizu i globalnu recesiju bar 70 godina stara ekonomska teorija, teorija koja gotovo ništa nije mogla da baštini ni od skorašnje literature o finansijskim krizama niti od skorašnjih (re)akcija multilateralnih finansijskih gardista, ipak je nemoguć pun oporavak od krize i ponovno uspostavljanje kontrole nad procesom ekonomske globalizacije bez odlučne i savremene reforme međunarodne finansijske arhitekture. Stoga, fundamentalno unapređena ekonomska trigonometrija na relaciji Međunarodni monetarni fond -i uglavnom zaboravljene- Svetska banka i Banka za međunarodna poravnanja, predstavlja verujemo potentniji i temeljniji predložak za praktičnu primenu međunarodne podele finansijske odgovornosti. U zaključnim razmatranjima, učinjen je pokušaj da se odstupi od normativne analize ne bismo li skicirali moguće ishode za krizom pogođenu svetsku privredu, s težištem na krucijalnim lekcijama iz nedavne prošlosti i nekolikim upozorenjima vezano za neposrednu budućnost.*
Ključne reči: : *međunarodna finasijska kriza, Londonski samit, G-20, reforma kvota u IMF, međunarodni zajmodavac u poslednjoj instanci, poreski rajevi, spoljnotrgovinski protekcionizam, kreiranje specijalnih prava vučenja, Bretton-Woods 2.0, loša reputacija IMF, svrha i zadaci BIS, repozicioniranje Svetske banke, globalni odgovor ekonomske politike, svetska privreda, upozorenja za budućnost.*

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"The market can stay irrational longer than you can stay solvent".

John M. Keynes

"Because we're all begging for aid, we just call it fiscal stimulus. And we're all begging for debt relief, we just call it disposing of toxic assets".

Sir Bob Geldof

"The human species, according to the best theory I can form of it, is composed of two distinct races: the men who borrow and the men who lend".

Charles Lamb

1. Introduction

Pending on their own traits, financial systems can serve as shock absorbers or, if the wrong screws are loosened, may innovate themselves into nasty amplifiers of havoc. For some people from global financial industry, regrettably, acquiring competitive advantage boiled down to making markets work less efficiently. One catastrophically diligent way of doing that is to start off myopically focused on circumventing capital requirements at the expense of long-run value creation, only to keep surfing on a deliberately raised asset-price tide whose ephemeral nature tends to be secluded by hidden or obscured information. Eventually, these days, professional community is more or less reaching consensus on what I argued in Malović (2008): Current international financial crisis could have been spotted from afar and should have been nipped into a bud as early as in 2002; that is, if we only had managed to push through a proper reform of international financial system resolutely and on time.

As is well-known by now, the crisis has been amplified by sky-rocketing food and oil prices, lax regulation of credit derivatives and cheap-money policy worldwide, but in my opinion, essential culprit of this latest global distress is choking overregulation of plain-vanilla banking in parallel with shocking absence of any regulation whatsoever of shadow-banking industry[1] and global OTC markets![2] While expanding aggressively or simply to keep up with their greedy competitors, international financial intermediaries spawned fancy asset-backed securitized monsters, which came in too many guises and ultimately got out of hand. Financial mutation brought about jitters of illiquidity across the industry and following the bankruptcy of Lehman Brothers on 15 September, triggered a systemic run in the inter-bank credit market, a paramount spike in corporate bond rates and a global loss of consumer and business confidence. Dramatic developments of the last 10 months or so have forced monetary and fiscal authorities around the world to open a second front in combating crisis–countering global recession. The result has been an unsurprisingly messy mixture of urgent and alarmingly unconventional treatment designed to stem the economic decline, combined with -an emerging, skittish and largely on paper still-agenda for a comprehensive reform to set the foundations for reasonably reliable global financial system and sustainable growth of national economies and world trade [BIS, 2009].

We are witnesses and victims of the fifth and by large the biggest international financial crisis in post-WWII. According to recent IMF (2009) estimates, direct deadweight losses of global banking sector are nearly 4.4 trill.US$, to put it into perspective, that amounts to 37 years of worldwide official development assistance at its 2008 level, with additional 1.5 trill.$ writedowns lurking ahead in 2009 and 2010![3] Fiscal costs of rescue efforts (surely well above 10% of their GDP for UK and US and somewhat lower for the rest of the world), already opening clearly unsustainable budget deficits, are to be added to the total bill. However, arguably the dearest cost of the crisis is represented by pecuniary equivalents of distressed stock markets, housing industry, huge unemployment, eurocurrency markets, bankrupt sovereigns and shaken credibility of price discovery function as such [Malović, 2008]. Having said that, can the world, in fact, even afford to fix the global financial system? The answer is yes, because we wouldn't survive another crisis like this one, because any neoliberal alternative would be penny wise-pound foolish, because Bretton-Woods system is years passed face lifting job and yearn for serious surgery... The question being, what is the wisest and sufficiently comprehensive way to do it [Wolf, 2009]?

The rest of the paper is organised as follows. Section 2 strives to take a closer look at the backstage nature and true measurements of the announced reforms as well as beef-up funds earmarked in the G-20's London communiqué. Section 3 goes into more detailed normative analysis both within and beyond the London summit in describing analytical and logistical tasks as well as solutions under the far-fetching umbrella of IFIs reform. Section 4 concludes with rather condense policy wrap-up only to submerge again into the gloomy junctions of crisis/post-crisis management that are laying ahead.

[1] Non-banking financial institutions of all sorts.

[2] See Malović (2008) for more detailed analysis on why subprime mess on its' own couldn't have caused a serious financial crisis in the US, let alone global meltdown!

[3] Out of which 950 bill.US$ of writedowns in remaining months of 2009 and 2010 are expected to take place in EU banking sector, which hints at greater difficulties in future financial deleveraging on this side of the pond [Goldstein, 2009], [Wolf, 2009].

2. G-20 and the London Communiqué

Gauged against despair of global recession just weeks before the G-20 gathering, the London summit appeared a spectacular, historically unifying and «full-figured» success in modern international finance. However, the summit paid no more than lip service to the grand Bretton-Woods conference of 1944. But, good news first. The London statement, quite rightly, contains strategic global consensus on the need for tougher financial regulation of non-bank intermediaries, globally coordinated fiscal stimulus, stronger and much more evenly governed multilateral institutions and reinforcement of market principles/globalisation benefits across the world economy [G-20, 2009]. G-20 deserves to be applauded for that. The eventual acknowledgement of the fact that the balance of economic power has irrevocably shifted and dispersed itself since the original Bretton Woods cradle[4], however justified and overdue, is a mighty achievement, embodied in the very volume of the new leading forum.[5]

Nonetheless, the London communiqué turned out rather heavy on zeros and ultra-light on substance, the result of its relevant proposals not being timely and vice versa. G-20 promised «concerted fiscal expansion» reaching 5 trill.US$ by the end of 2010, as well as swift 1.1 trill.US$ injection of readily available resources through IMF, additional 100 bill.US$ development lending via World Bank and alike, together with 250 bill.US$ package aimed at propelling foreign trade finance [*Ibidem*]. Also, following US Congressional approval, IMF intends to sell 403 metric tons of monetary gold in order to increase the Fund's liquid reserves [Sanford-Weiss, 2009].

G-20's intention to beef-up and revive the IMF from virtual irrelevance to global fire-fighter and crisis-insurer seems genuine enough. However, pompously advertised tripling of IMF's resources to 750 bill.US$ plus 250 bill.$ of newly created Special Drawing Rights (SDR), IMF's quasi-currency, is hardly enough to erase economic memory of the developing world. After the Fund's role in the emerging market crises of the 1990's, ranging from spectacularly useless to positively harmful,[6] LDCs started hoarding FX reserves so as never again to fall prey of IMF's sometimes reckless conditionality attached to new lending. It is of secondary importance that this constellation financially and ideologically dwarfed the Fund. More importantly, the London communiqué only implicitly admitted that the IMF's ignorant and/or merciless conditionality lending co-starred in a chain of events that created this latest financial crisis in the first place![7] If aiming to deliver vis-à-vis G-20's ambition laid out at the onset of the passage, IMF would have to regain professional and moral legitimacy by distancing itself from G8, yet it cannot afford to waist the monetary and political support of the advanced countries which still form the majority of its shareholders [Pisani-Ferry, 2008]. In spite of many reforms under way (some of which, honestly, begun much before and irrespectively from G-20 summits[8]), XXI century IMF still escapes even the implementation of already enforced- let alone discussion on the more deeply rooted transformations. We shall return to this point a bit later.

Be that as it may, thanks to London summit, at least the Fund's saddlebags came out full of nuggets, i.e. as one Oxfam activist said: "IMF is big, bad and back"…or is it? Out of announced 500 bill.US$ extra money, 250-300 bill.$ was probably already in the pipeline, hence, isn't really additional. Furthermore, 1.1 trill.$ of earmarked resources is financing, not at all guaranteed to produce a trillion of additional spending [Subramanian, 2009].[9] Worse still, microfinance analysis of G-20's dealing with IMF's supply-side remains somewhat puzzling. At the G-20 meeting in April 2009, the major countries agreed that the resources of the New Arrangements to Borrow (NAB) should be expanded by about $500 billion. However, some of the beef-up funds were already committed to at the time of London summit (Japan's 100 bill.$ and EU's 102 bill.$), whereas contributions of other countries remain partly undisbursed (US promised 100 bill.$, China 40 bill.[10], Switzerland 10 bill., S.Korea and Canada 10 bill.US$ each and Norway 4.5 bill.). The sources for the remaining 125.5 bill.US$ supplemental funds have not been identified yet [Sanford-Weiss, 2009]. Obviously, China could

[4] Or indeed since the contemporary G-8 likewise...

[5] Unlike Mr. G. Brown, I wouldn't go as far as announcing death of «Washington consensus» policies, but emergence of G-20 as the manager of world affairs is hopefully an anti-trust fullstop on US monopoly over both resources and ideas to reform the international financial system.

[6] IMF's deregulate, liberalize and privatize ideology back-fired in Argentina (the "Washington consensus" transition champion) and stalled development in much of L. America, while IMF's austerity policies of spending cuts and interest rate hikes during currency crises in South-East Asia either exacerbated the meltdown, or in the words of its own evaluation of the mission in 1998 Indonesia, resulted in a collapse which "makes it difficult to argue that things would have been worse without the IMF".

[7] In order to avoid the crushing arms of the Fund's programmes, many emerging markets deliberately run BoP surpluses, thereby contributing to -what B. Bernanke dubbed- «savings glut», a flipside of global imbalances which unleashed liquidity boom (official reserves nowadays do not sit idly in central banks' valts) and short-sighted innovation within international financial industry in finding ways to exploit it- including the whole menu of subprime loans and contaminated assets [Bernanke, 2008], [Obstfeld, 2009].

[8] See, e.g. IMF (2008).

[9] It was A. Marshall to be the first pre-Keynesian to realize that "though men have the power of purchase they may not choose to use it" [Blaug, 1999, p.152]. On the other hand, Subramanian (2009) warns that 60% of freshly created SDR liquidity will go to rich countries which do not really need them, at least without worked-out procedure for reallocating them further onto the poor(er) IMF members. Therefore, even absent obstacles on demand-side, these funds shall have little immediate effect on spending.

[10] China shall provide her 40 bill.$ possibly through SDR bond purchases [Sanford-Weiss, 2009].

easily give out more together with expected commitments of Saudi Arabia and other major emerging markets [Subramanian, 2009], but their hesitance has a lot to do with still remarkably superficial IMF quota reform[11]. Instead, G-20 offered to loosen EU's grip on the appointment of IMF managing director [The Economist, 2009]: timely but pretty irrelevant proposal.[12]

Suggested amendments to the existing distribution of IMF votes are, alas, rather cosmetical: e.g., for the US 16.73% instead of 16.77, for China 3.81% instead of 3.66, for Brazil 1,72% instead of 1,38. After G-20's supervised quota reform, for instance, Belgium with less than 50% of S.Korea's GNP retains 50% more representation at the IMF! For the time being, the only non-negligible voting right amendments are involving France, UK (both downward) and India (upward). However, London communiqué failed to address the recommendation to cut the required percentage of majority votes needed to reach crucially important decisions within the IMF: from existing 85% to 70-75% [The Economist, 2009]. Proposed quota reform, in fact, leaves the US veto effectively out of reach.

In addition, let us reflect upon motivation and conceptual flaws of the G-20's policy response in other designated areas: coordinated fiscal stimulus, tax heavens, protectionism and trade, financial regulation.

First of all, there was no overly concerted fiscal expansion to speak of, and to make it more ambiguous as a goal, two OECD economies with currently brightest recovery prospects are Germany and Japan, first markedly lagging behind and second being at the forefront of fiscal expansion bandwagon.

Tax heavens appear to be even more of a disappointment: before the London summit, I thought that regulators were meant to work multilaterally on a core set of prudential/auditing issues in order to disable global banks' presently evident ability to hand-pick their optimal (typically off-shore) jurisdictions. Slipping off the politicians' tongues, it afterwards turned out that cracking down on tax heavens agenda was there only to secure national tax bases (staying put), whose levies are supposed to repay the ongoing fiscal stimulus.

Moving on to trade finance issue, G-20's 250bill.US$ to be provided via WTO and export credit agencies is probably a wee-bit late and could scarcely do more than neutralize already horrific consequences of recently re-erected trade barriers.[13] Now, dried-out export credit may well be part of the problem, but throwing 250bill.US$ at it is no substitute for political will to resist protectionist pressures [Subramanian, 2009]. This even more so since 4/5 of money circulates through export-supporting agencies, which in crisis times might be tempted to pick and favour 'national champions' once again, igniting thereby the race to the bottom.

In respect to financial regulation reform, G-20 leaders were loud and clear on imperative of including systemically important hedge funds and credit-rating agencies into entities to be screened, on making derivatives tradable in organised markets, the need to revise accounting rules etc. [Williamson, 2009]. However, despite they ended up being innocent victims, to what extent will emerging markets and LDCs realistically have a say in global financial regulation redesign this time?[14] Moreover, there was no recognition whatsoever of the pressing need to discourage financial intermediaries from making themselves too-big-to fail and to penalize those with alarming maturity mismatches [Williamson, 2009]. Having said that, regardless of how relevant it may be, the immediate fiscal cost of the ensuing bail-outs is not the principal objection here. Namely, if we are socializing the costs while privatising the profits it is reasonable to expect a limited number of influential, complex financial giants to emerge shortly. Their depositors as well as creditors would naturally believe they were lending to governments- a recipe for yet bigger cataclysm in the future [Obstfeld, 2009], [Wolf, 2009].

Finally, G-20 leaders expressed their environmental sensitivity notwithstanding the fact that a few months earlier Kyoto-inspired environmental protection funds had been the first virtuous casualty of the global crisis. Apart from appearing "green", London summit postponed any actual decisions for Copenhagen meeting in December 2009.

At the expense of being cynical, perhaps the biggest achievement of the London conference and the only thing G-20 leaders whole-heartedly agreed upon was that they should meet again [Subramanian, 2009]. Therefore, the next section sketches more comprehensive proposal for reform of IFIs, goes into more technical details regarding some vague G-20 blueprints, as well as sets out several propositions not mentioned at all in the London communiqué.

3. Towards Bretton-Woods 2.0

History has shown that crises present admirable opportunities to redraw old arrangements [Ocampo, 2009]. However, "the reality is that changes in the international financial architecture are almost always incremen-

[11] Quota is basically the funds origin, contributed by IMF members, which defines the participation rate, voting power as well as maximum borrowing capacity of a country.

[12] See, e.g. Fratianni and Pattison (2004)

[13] In March 2009, according to WTO estimates, global trade flows plummeted 9% and thus recorded the deepest year on year fall in the post-war period. At the Washington summit in November 2008, consensus was reached not to restrain to protectionist trade policies at the verge of global recession. Within weeks, 17 out of 20 G-20 members resorted to either antidumping measures or various other trade restrictions (Russia raised tariffs on used cars, India pushed up tariff on steel, China banned imports of certain EU beers and Irish pork etc.)

[14] Pissany-Ferry (2009) reminds us that US and Europe jointly represent 70% of global supply of financial assets and over 70% of financial regulation. This would suggest that managing financial crisis and especially preventing future ones may essentialy stay a transatlantic affair.

tal" [Eichengreen, 2009, p.5]. Hence, I oppose uneconomical creation of entirely new financial organizations and advocate rescuing and reorienting the existing ones, with particular attention to IMF's two forgotten siblings: an older relative, BIS, and its twin sister, IBRD (nowadays the World Bank). In what follows, I shall describe the roles for each one of the three coupled with principal controversies regarding individual topics under their respective responsibility. The world is in desperate need for the Bretton-Woods 2.0. In fact, if we fail to address financial regulation/reform issues urgently, soon enough we shall have the Global Financial Meltdown 2.0 instead.

First of all, we must resist temptation to turn the IMF into singular mega-institution assuming all the global financial affairs at hand. With the end of the old par system, much of the Fund's activity shifted to surveillance of exchange rate policies and global imbalances, as well as to dealing with occasional BoP, currency and international debt crises stemming from mostly macroeconomic mismanagement.[15] Therefore, Fund should continue what it does best: being primarily concerned with sovereign countries. In order to *1)* remove its stabilization policy stigma, IMF should put his money where its tongue is recently laid. If determined to fulfill international monetary stability goal, IMF would have to devote more of its effort to preventing both involuntary and intentional currency misalignment corollaries, preferably via *2)* expanding role of SDR as the utmost diplomatic toolkit. Clearly, to live up to our firefighting expectations in increasingly turbulent times, IMF must *1)* reclaim its role of international lender of last resort (ILOLR), feasible only hand in hand with its potential rival, the Bank for International Settlements (BIS)!

What ought to be done for the stigma to be removed? Undoubtedly, IMF should credibly recoup legitimacy of its governance structure and repair affordability and policy reputation of its credit facilities. Instead of postponing more ambitious quota reform for 2011 (by which time pressures for reform will probably dissipate) [Subramanian, 2009], Fund should deal with perhaps too many and undeservedly powerful European seats as well as the US voting monopoly without further delay. The new quota formula dispensing with mind blowing combination of the previous five[16] is much better balanced move, an indication that the Fund was trying to inspire some endogenous reforms even before the emergence of G-20. Similarly, a step in good direction is Executive Board's 2008 recommendation to triple so-called basic votes of IMF members, to amend for successive increases in quotas which actually silenced the voices of small(er) countries from 11% (in 1945) to 2% (in 2008) [IMF, 2008]. Honestly, IMF is in dire straits here. More immediate and luckily more feasible attention, however, is required in carrying out already publicized reforms and orders given by IMF's top management. Newly created FCL (flexible credit line) is meant as a precautionary lending facility designed for well-performing emerging economies,[17] not for the struggling and badly infected ones mentioned in IMF's verbal interventions! As a matter of fact, the entire G-20 earmarked only 50 bill.US$ as a help for poorest part of the world, collaterally damaged by the global depression. IMF's contribution is destined to be even more modest, since intended gold sales over patty-cash won't do much good because the great deal of funds will be swallowed by the its' own operating budget [Sanford-Weiss, 2009]. Absence of «even-handedness» is, alas, not striking in quantity alone. IMF has been preaching the use of monetary rules for decades now, while the Fund itself is still relying on bad old discretion. For instance, by mere reviewing its last nine stand-by arrangements negotiated since the september 2008 reveals much the same neoliberal shambles that gave it bad reputation to begin with! All of the arrangements ruthlessly «provide for spending cuts, despite the IMF's avowed commitment to a worldwide fiscal stimulus» [Weisbrot, 2009, p.2]. Keynesianism is back in fashion, but only for large shareholders?! [18]

Ever since the Triffin Dillema initially released the idea, there were two underpinnings of SDR creation.[19] One was - growing supply of global liquidity without weakening confidence in greenback[20], the other - enabling "long-term structural improvement in the world monetary system", or the mirror image of increasing the portfolio choices available to reserve holders [Eichengreen, 2009], [Williamson, 2009*]. I think the both arguments are relevant, although the latter more immediately so. Therefore, IMF should include renminbi in the structure of SDR, institute an obligation for central banks around the world to stabilize their currencies in terms of SDR and engineer two-way substitution accounts through which portfolio rebalancing would take place. Nevertheless, an expanded

[15] Multinational banking crisis, international financial market crashes and meltdowns originating from global derivatives industry, are systemic incidents for which detection and taming the Fund obviously doesn't have the capacity to credibly assume such a role [Tarullo, 2007].

[16] The new, simpler and more transparent IMF quota calculation, $CQS = (0.5Y+0.3O+0.15V+0.05R)^k$, relies on the weighted sum of four variables (GDP, trade openness, variability of receipts and capital flows and lastly, annual average of reserve holdings) corrected with compression factor which reduces dispersion in calculated quota shares [IMF, 2008].

[17] Not surprisingly, strategically sensitive Mexico, Columbia and Poland were the first economies to secure it. *Stricto sensu,* even FCL is free only of structural conditionality.

[18] At the same time, the IMF is apparently silent on the US budget deficit being doubled within a year or US public debt surging 15 percentage points within less than two years.

[19] SDR is currently defined as liquidity basket consisting of US$ 44%, EUR34%, JPY and GBP 11% each. The basket is recalculated every 5 years. Interest rate on SDR is around 0.6%. Before the London summit, there were 21.4 bill. SDR in existence, less than 0.5% of the world's non-gold reserves [Williamson, 2009*].

[20] As a matter of fact, without detrimental appreciation of the euro either, because that's what the conversion would otherwise flow into.

role for the SDR would have to appoint the IMF to act as market maker and subsidize bid-ask spreads until the market gains momentum [Eichengreen, 2009]. In as much as proposed measures give impetus to private market for SDRs, they might be held both as denominators to facilitate transactions and as an interest bearing asset [Williamson, 2009*]. That would unambiguosly reduce the harshness of global BoP imbalances. Even if one disregards more egalitarian distribution of international seignorage under the dollar-SDR reserve system, such a development may even entirely crowd out the dollar as the leading reserve currency in the more distant future.

The current financial crisis has witnessed bank bailouts of previously unthinkable proportions. As a consequence, the design of the institutions that govern bailouts has moved to the forefront of the political debate [Agur, 2009]. Theoretically indisputable arguments for IMF acting as an ILOLR are examples of individual macroeconomic crashes leading to spill-over cascade of otherwise avoidable overseas defaults or perhaps less catastrophic international repercussions of national monetary policies. Nevertheless, Obstfeld (2009) warns how hard it is to escape the conclusion that ILOLR powers must -one way or the other- be vested with centralized agency which both supervises[21] global financial markets on a consolidated bases (e.g. BIS), and is able to internalize other externalities arising from national exercise of LOLR function (e.g. IMF). To put it bluntly, the centrality of the IMF is gone [Pisani-Ferry, 2008], since the ILOLR task is impossible without helping hand of the global banking watchdog. Unlike "the central bank of central banks", IMF has neither experience nor established channel of communication with financial markets. Moreover, generalized financial distress cuts into the responsibility barbwire between each national LOLR [Obstfeld, 2009]. In order to stop international financial contagion, there's a clear cut case for the IMF as a global emergency lender, yet not alone nor broke any more.[22]

BIS has a natural role to play in prudential regulation cum supervision of global financial markets. Logical starting point in recapturing that role is reform of its Basel II standards, primarily spectacular failure of IRBS and credit-rating methodology of leading global rating agencies[23] [Tarullo, 2008], [Sy, 2009]. Equally crucial, weaknesses in underwriting and upgrading procedures need urgent attention of BIS![24] In that spirit, Huang and Ratnowski (2008) simulated events leading to the credit crunch as aggressive expansion of financial sector through wholesale funding, precisely due to voluntaristic, too arbitrary credit-rating and unreliable risk-assessment. In turn, at the refinancing stage, there was a risk of wholesale funds being abruptly withdrawn on a hint of negative news, triggering inefficient liquidations [*Ibidem*]. Hence, as the most obvious institution for the job, BIS must organize and enforce Goldstein's (2009) obligatory additional capital charges on recklessly expanding, systemically important financial intermediaries, whatever they call themselves.[25] Together with IMF, BIS should develop procedures for calming Fisherian debt deflation scenarios by postulating the rule under which noosed debtors in global recession have to pay only the PPP equivalent of the nominal debt plus accruing interest![26] Moreover, Grauwe (2009) recently exposed another malpractice of credit-rating agencies: continuously giving more favourable rating to sovereign debts of countries with more liberal models of economy. The rationale behind it was that flexibility (of easier downsizing, sacking etc.) gives them a better capacity to adjust than to rigid more expensive welfare oriented states. Indisputably, more liberal economies will spend less on unemployment benefits and other interventions, yet to the extent that Fisherian debt deflation bites deeper into the economic activity of liberal states, public revenues might decline comparably more. Consequently, budget deficits may actually increase less in

[21] Just as it's not desirable over the long run for the FED to stand as an ILOLR (via mewly florished swap lines) for financial intermediaries over which it has no direct supervisory power, the same goes for the IMF. Lending between central banks and lending to troubled banking systems requires careful international coordination and close cooperation of the central banks, multilateral macro- and micro-watchdogs, the IMF and the BIS.

[22] However, when it comes to international (systemically important) banks rescue, there are no golden rules and ready-made solutions here: see Agur (2009) for extensive review of constellations under which different sets of centralization, decentralization or indeed delegation of (I)LOLR may be optimal. As M. King of Bank of England said, modern banks tend to be "global in life but national in death", which is why politicians still often reject the burden-sharing scheme that would commit their voters/taxpayers to rescuing non-national banks [Pisani-Ferry, 2009]. Even if they don't have narrower objective functions, LOLR may have informational supremacy and thus signaling advantage over ILOLR, especially if the latter does a sloppy job. But, unforeseen by Agur (2009), vice versa also holds: if LOLR does a lousy job and/or ILOLR has a more selfish objective function, ILOLR might have a signaling advantage too! In addition, if LOLR is engaging in window-dressing, coordination cannot possibly replicate centralization [Agur, 2009].

[23] Sy (2009) illustrates how financial markets over-relied on ratings and, in return, how downgrades have led to systemic market losses and liquidity squeeze. Worse still, rating agencies consider themselves answerable for assessing credit risk solely, whereas investors typically reckon with liquidity risk being accounted for in leading agencies' ratings too. [Malović, 2008].

[24] As a matter of fact, the metric used for structured product rating has been identical to methodology used for simple bonds [Malović, 2008].

[25] Less obvious model of orchestrated self-insurance of global banking industry, but similar in fashion, is H.W.Sinn's regulatory proposal for amending the valuation failures of mark-to market accounting: company's assets should be valued according to the lower (of historical and current) value principle at tranquil times already, so that bubbles get deflated on the runaway rather than being kept artificially overvalued in the midst of crisis [Malović, 2008].

[26] This proposal bears elements of bail-in quality towards the international banking community without endangering its capability of staying in business.

more expensive welfare economies [Grauwe, 2009]. Therefore BIS has to make sure that we have as accurate as possible credit-rating methodology, by re-regulating, monitoring, and spurring competition between the leading credit-rating agencies in the world. But that might not be sufficient on occasion. Besides regulation and supervision of international banking and global derivative markets, BIS must stand ready for banking crisis management including establishment of multilateral insolvency trust for global banks.[27] However, flickering nuance between illiquidity and insolvency amidst planetary financial distress provides us with yet another caveat: Aizenman (2009) in his latest paper formally models one of the key arguments in Malović (2008), that too much regulation proves just as detrimental to international monetary stability as the incredibly imprudent lack of it.[28] Perhaps the best illustration of the point just made is the key finding of Amenc and Sender (2009): mere acknowledging that banking capital ratios fall during downturns would have made most of the unprecedented fiscal injections immaterial! Instead, the world embarked on the notorious, internationally uncoordinated and bulky vehicle of fiscal injections: from outright recapitalization of private banks, through explicit guarantees of private liabilities to help banks to keep abreast with wholesale funding needs, all the way to government sponsored purchases of impaired quality assets [Panetta *et al.*, 2009], [Swagel, 2009]. And the bank rescue, I dare say, is muddling through at best. Oddly enough, history of banking crises seems to be indicating that for as long as there's credit and demand picking up somewhere, banks could even remain lingering for a while in parallel with initially robust recoveries of the "real" economic activity.

But, say that national fiscal stimuli didn't do the trick?! What if, following Rodrik (2009), there's no import demand for LDCs' tradables due to global BoP adjustment and/or dealing with so-called twin deficits? What if the middle and low income economies most likely won't qualify (or indeed won't apply) for IMF's Flexible Credit Line? This is where the World Bank kicks in. My thesis is that in fact, in a demand-driven crisis, growth and development should be of principal concern, rather than international monetary stability.[29] Moreover, the only way out is growing out of crisis: hence, the leading role in lending, SDR liquidity creation and in drafting the individual anti-crisis strategies for LDCs ought to be performed by the World Bank, not the IMF or the BIS.[30] WB's infrastructural and growth-oriented lending would be patently stimulating the aggregate demand, while somewhat obscuring the tranquil or turbulent motivation of its borrowers. Greater precision combined with less or no negative signalling married in World Bank lending could (have) conceivably even lower(ed) the fiscal cost of the global dirigisme, as well as shorten(ed) and dilute(d) the exotic voyage of US monetary easing. This U-turn in the World Bank's strategic positioning, however, counts on considerable financial and intellectual firepower yet to be obtained, partly at the expense of fiscal loose cannons and heavily biased financial boost of the other Bretton-Woods sibling.[31]

Hence, a fundamentally upgraded economic trigonometry among the IMF, (followed by the largely neglected) World Bank and BIS is put forward as a hopefully more able and further reaching proposal for policy oriented responsibility sharing.

4. Concluding remarks: lessons learned vs. caveats ahead

I ventured to accomplish three goals in this paper: First, to unwrap and bring out the "Rasputinean settlement" traits of the G-20's London Communiqué. Hopefully, I managed to expose the (un)official economic reasoning underneath highly political tongues. Second, to pave the normative pathway towards Bretton-Woods 2.0, a radical yet traditionally vested reform of global financial guardians. To that end, I sketched a tripartite international financial architecture filled with handful of more detailed topics that depict analytical Q&As for various responsibilities of the institutions these are or should be assigned to. My idea of Bretton-Woods 2.0 resembles a revolver barrel whose three different caliber chambers are rotating along with the nature of economic problems the world might be facing, their chief duties being clearly defined but details and tactics not cast in stone, so that pending on micro or macro, sovereign or banking, recessionary or stagflationary origins of the crisis, each of the three institutions could be spear-leading the global policy response. Third, to draw quick lessons and confront them with couple of caveats that may be lurking ahead.

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27 See Eichengreen (2009) for more details on insolvency trust for international banks.

28 I myself claimed that we had simultaneous compact of both over- (in traditional banking) and underregulation (elsewhere in financial industry) reflating the bubble across the range of asset classes to the point of pricking. In contrast, Aizenman (2009) accentuates intertemporal dimension to it, by saying that higher regulatory effort, while helping avoid a crisis, may be confused as a signal that the environment is less risky, thereby eroding future regulatory efforts. The recessionary side of the regulation paradox is assertion that crisis resulting in unexpectedly high costs may induce over-regulation and economic stagnation [Aizenman, 2009], an extreme that the BIS must not succumb to.

29 IMF's notorious and procyclical conditionality set aside, so many times before countries either restrained from borrowing the Fund's contigency money - since that would be typically read as the sign of fairly terminal macroeconomic illness (followed by capital-flow reversals), or indeed have borrowed from the IMF - only to watch their private creditors' risk premia soaring over the Fund's indisputable seniority [Stiglitz, 2002].

30 See Linn (2009) for similar albeit less radically articulated proposal.

31 Both IDA and IBRD eligibility bars should be raised in the process. The Bank's research staff, at that, should be much more concerned with WB-programmes evaluation, rather than with abstract scholarly publications [Tarullo, 2007].

For one, we should've seen this coming. Virtually every country experiencing financial crises of the 1990s had an untenable friction between financial superstructure and performance of the real economy [Cooper, 2002]. Hence, OECD economies demonstrated they could be every bit as fragile as emerging markets thus far: not only overvalued national currency, but -why not- a collapsing price of any other widely held asset can and, chances are, will erupt in widespread financial distress [Obstfeld, 2009]!

Properly reformed IFIs ought to be capable of mitigating the future crises, yet if would be against the odds to claim that regulators may ever outstrip the pace of international financial innovation. The name of the game is not being too far behind.

Moreover, success of banks' nationalization and lasting recovery of global banking has always depended on getting some air back into burst asset bubbles which define their net worth, hence there's no room for nagging about light on financial horizon being lit by liquidity bubble. In a liquidity trap, it would be nasty if there were none. The crunch seems to be slowly dissipating. However, it might be too soon for toasts: in both Great Depression and the current crisis credible upward trends were recorded only to dwindle in a free fall yet again. Apparently, "paradox of thrift"[32] is here to stay; on top of swift reforms and cautious policy-making, world will need a bit of luck to loosen its grip. Having said that, few caveats are in order.

If the crisis persists, it might become resilient to crowding in private investment via altered structure of central banks' balance sheets cum fiscal expansion: sizable inflation could be the only drug on the shelf then, albeit with many unpleasant side-effects.

If we weather the crisis, we may easily end up sucked in the orbit of another one. International orchestration of practically simultaneous fiscal and monetary restriction is going to be formidable stumbling block before we really see the end of this.

Either way, stagflation might slip in on a tide of repeated bank run, contracted supply-side shock and the loss of confidence. And frankly, there's no drug in the pharmacy for that yet. So, it's still fragile out there –handle with care.

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