IS GLOBAL FINANCIAL GOVERNANCE STILL POSSIBLE?

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ABSTRACT

Historically finance has been shaped by crises. This paper attempts to shed light on the causes of and policy responses to the 2008 Lehman shock and its aftermath as well as the 2010-2012 eurozone crises. The former has led to the creation of the G20 and the latter the emerging banking union. But these new institutions would probably not suffice to give rise to more robust global financial governance. This is probably because of the growing financial clout of China and other major emerging nations that have only recently created a new development bank. In the circumstances, realizing more robust global financial governance seems getting more difficult.

Keywords: global financial governance. Lehman shock, eurozone. crisis, BRICS, AIIB

Introduction

Global finance has been shaped by crisis since the late 18th century .The crises have given rise to such institutions as the U.S. Federal Reserve and the deposit insurance institution (FDIC). In other words crises in global finance and its rebirth have been closely intertwined.

This paper attempts to shed light on causes and policy responses to two of the recent major crises--the Lehman shock and the eurozone crisis--and rethink lessons from them Such an exercise should help to devise more robust and resilient global finance. In other words, the author is eager to know whether global financial governance is still possible.

Here is the definition of global financial governance; the broad fabric of rules and procedures by which internationally active financial institutions are governed, while the architectural elements of governance should include the public mechanisms by which authoritative decisions about these rules and procedures are made (Germain, 2001).

First the author reassesses the viability of of the Bretton Woods institutions--the International Monetary Fund (IMF) and the World Bank--and mulls on their achievements as well as their relevance and limitations in the wake of the Lehman Shock and the eurozone crisis. In particular, there will be focus on the reform of the IMF through voting rights reallocations and the Group of 20 (G20) major countries born amidst the Lehman shock conflagration. In connection with the

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IMF reform, China and four other major emerging nations called the BRICS are apparently frustrated and decided on the creation of their own development bank and a fund.

The author analyzed causes of the Lehman shock and pointed out three harbingers of the crisis: 1) surge in debt, especially in the financial sector resulting from a housing bubble, 2) complex interconnections of securitized finance with no one having clear understanding of what assets were worth or who owned what, and 3) uncertainty about a safety net (*Economist*).

As regards the eurozone crisis, the author identified its three intertwined aspects: 1) fiscal and sovereign debt crisis, 2) bank crisis, and 3) growth and competitiveness crisis.

The EU and the eurozone have come up with strategies to overcome the crisis situation and to prevent its recurrence with an emphasis on the banking union, fiscal union and further economic integration to boost growth. This paper attaches importance to the fledgling banking union.

Revolts are spreading in the international financial system against a global economy characterized by open markets, unrestricted capital flows, and the activities of multinational firms.

To remedy such a situation, the author argues that a new, more, just and sustainable international economic order should be built, which includes, among otherthings, mechanisms to combat poverty, to solve environmental crises, and promote human development in areas including health, education and housing.

In the concluding section, the author will attempt to answer the question "Is global financial governance still possible?"

2 History of crises that shaped finance

The history of finance is strewn with episodes which shows that "finance is not merely prone to crises, it is shaped by them." (*Economist*).

This chaptertraces five disasters, from 1792 to 1929that illustrates the origins of the modern financial system. Included are hugely successful the Federal Reserve, the New York Stock Exchange and the Federal deposit insurance system.

There are five crises:

(1) 1792: The foundation of modern finance

Speculative fevers in New York and Philadelphia thatwent bust. There emerged an agreement that finance had become too frothy. Seeking to protect naive amateurs from risky investment, lawmakers sought outright bans, with rules passed in New York in April 1792 outlawing public futures trading: In response to this aggressive regulation a group of 24 traders met on Wall Street --under a buttonwood tree, the story goes--to set up their own private trading club. That group was the precursor of the New York Stock Exchange.

(2)1825 : The first emerging market crisis

Britain's response to the 1825 crisis involving new countries in Latin America that had broken free from Spain, such as Colombia, Chile, Peru, Mexico and Guatemala. Britain became a world leader in banking and bonds.

(3) 1857: The first global financial crisis

Involving railway share fever, it started in Ohio and then spread to New York and then to British cities, including Glasgow, Liverpool and London. On top of being global, the crash of 1857 marked another first: the recognition that financial safety nets can create excessive risk-takin

(4) 1907: Emergency money

Two greedy scammers--Augustus Heinz and Charles Morse--had borrowed and embezzled vast sums in an attempt to corner the market in the shares of United Copper. This eventually embroiled a trust company, Knickerbocker Trust. A plan for $500m official emergency money was quickly put together.

Following the 1907 disaster, the United States decided to set up proper lender of last resort: the Federal Reserve

(5)1929: the big one.

In the New York stock market crash on Oct. 28-29, the Dow Jones stock average lost close to 25%. A total of 1,359 banks failed that year. There were banking panics in Austria and Germany. The first step to de-risk the financial system was a massive injection of publicly supported capital amounting to $1billion.To neutralize future risks, the Glass-Steagall new rules were legislated to separate stock market operations from more mundane lending operations. Moreover, the Fed was given new powers to regulate banks whose customers used credit for investment. A new government body was also established to deal with bank runs once and for all: the Federal Deposit Insurance Corporation (FDIC).established on Jan. 1, 1934.

Crashes were caused by "blind capitalism": credulous cash, ignoring risk, flooded into unwise investments(Bagehot). This has prompted governments to devise some special rules to make finance safer. Bagehot insisted on the need for cenral banks to rescue banks during crises.

3 Bretton Woods revisted

The Bretton Woods agreements that led to the creation of the IMF and the World Bank were signed 70 years ago. The two institutions have been instrumental in usheringin a long and relatively peaceful period of economic growth.

Under the Bretton-Woods system, capital controls and fixed exchange rates lasted until the 1970s.

While the Bretton-Woods system has proved enduring, the balance of economic power between the west and emerging countries has substantially shifted with the former's share in the world economy dwindling

The U.S. Congress had long resisted the expansion of China's IMF voting rights. But it finally changed its hardline stance on China in December 2015 when it passed legislation approving long-pending quota reform of the IMF that will give more voting rights to emerging economies like China and India in the functioning of the organization.

The IMF Quota and Governance Reform would marginally reduce the voting share of traditional economic powerhouses like the United States.

On the other hand, China will have the third largest IMF quota and voting share after the United States and Japan, and India, Brazil and Russia would be also among the top 10 members of the IMF. China's quota will increase from 3.996% to 6.394%, making it the third largest shareholder in the IMF from the sixth.

The reform is a much better reflection of the state of the world economy.

Earlier in December 2015, the IMF took another step to integrate the Chinese economy into the world's financial system in view of its importance as the world's second largest economy.

The world organization decided to include the Chinese currency renminbi (RMB) or yuan in its basket of reserve currencies called the special drawing rights (SDR). The decision is regarded as

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both recognition of the increasing role the RMB plays in international finance as well as a vote of confidence in China's economic reforms.[1]

The IMF move is intended to nudge China toward greater further liberalization as much as to reward Beijing's past performance.

The IMF created the SDRs in 1969 as a way of increasing global liquidity. At that time, many countries tied the value of their currencies to the dollar. But the only way for them to get dollars was to have the U.S. government print more money-a process that risked undermining the value of the dollar. The SDR gives member countries access to another ready currency in the event of a balance of payments crisis.

China welcomed the IMF's decision, saying "it means the international community has greater expectation on China to play an active role in the world economic and financial arena." This will necessitate, among other things, greater transparency in decision making by the People's Bank of China than has been the norm.

The following are monetary milestones as described by *The Economist* with focus on the Bretton-Woods institutions:

1871 Germany joins Britain on the gold standard, most

of the large economy follow suit

1914 Outbreak of war brings to an end to the classical

gold standard

1923-27 Countries stabilize their exchange rates and

restore gold convertibility

1929-36 Gold standard gradually abandoned again

1944 Bretton Woods establishes a new fixed exchange

rate system

1959 End of postwar foreign exchange controls

[1] ***The Japan Times*** **editorial, "IMF's vote of confidence in RMB", Dec. 5, 2015**

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1967-73 Collapse of Bretton Woods (U.S. ends gold

peg, most countries begin to float

1979 European Monetary System (EMS) established 1992 Britain and Italy forced out of EMS

1999 Euro adopted

2008 Lehman shock

2010-13 Eurozone crisis

4 Lehman Shock that gave rise to G20

Three harbingers of the disaster of September 2008 can be observed in terms of vulnerabilities *(Economis*t):

1) surge in debt, especially in the financial sector

resulting from a housing bubble

2) complex interconnections of securitized finance: no one

understood what assets were worth or who owned what

3)uncertainty about a safety net

Meanwhile, global forces were apparently behind the crisis: the bursting of the property bubble in the United States and the ensuring contamination of balance sheets of financial institutions around the world, excessive leveraged positions both in the United States and Europe.

Rampant optimism that led to the Lehman disaster was fuled by a belief that macroeconomic instability was eradicated. Low and stable inflation and sustained growth spawned a perception of low risk and high return on capital (Van den Noord and Szekely, 2011).

From a historical perspective, the recession in the 1930s lasted longer and spread at a slower speed across majoreconomiesthan the Lehman collapse-triggered crisis.

On the other hand, today' s collapse in trade, fall in asset prices and downturn in the real economy are faster and more synchronous than during any previous global crisis.

The high speed of information flow via new communication technologies and the unprecedented degree of real andfinancial global integration partly account for this. Also the speed of financial innovation and the extent of leverage made for sharp adjustment when financial markets turned down. (*Economist*).

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The birth of the G20 summit was triggered by the Lehman shock. In November 2008, the leaders from 20 of the world's largest economies were invited to the first G20 summit in Washington. They agreed on a Joint Action plan for dealing with the crisis, including measures to reinvigorate their own economies (without damaging global trade), to regulate global finance, to assist poorer countries affected by the crisis and to reform global institutions.

The G-20 process was a shot in the arm not just for coordination among governments but also for existing multilateral institutions--and in particular, the IMF. (Woods, 2010).

This paper also focuses on the overhaul of financial regulations since 2008:

1) new Basel capital standards (obligations to hold more

and better capital relatie to assets),

2) the pushing of derivatives trading onto clearing

houses,

3) improvements of transparency

Global finance is safer, but not safe enough *(*Economist). Massive bailouts from governments and central banks staved off a second Depression, while the banks have raised more capital and written off more dud assets than most others. (ibid.)

Of course, morale hasard cannot be denied. Because investors know the state will bail out banks, parts of finance have become a one-way bet (*Economist*).

5. Lessons from the eurozone crisis and an emerging pan-European banking Union

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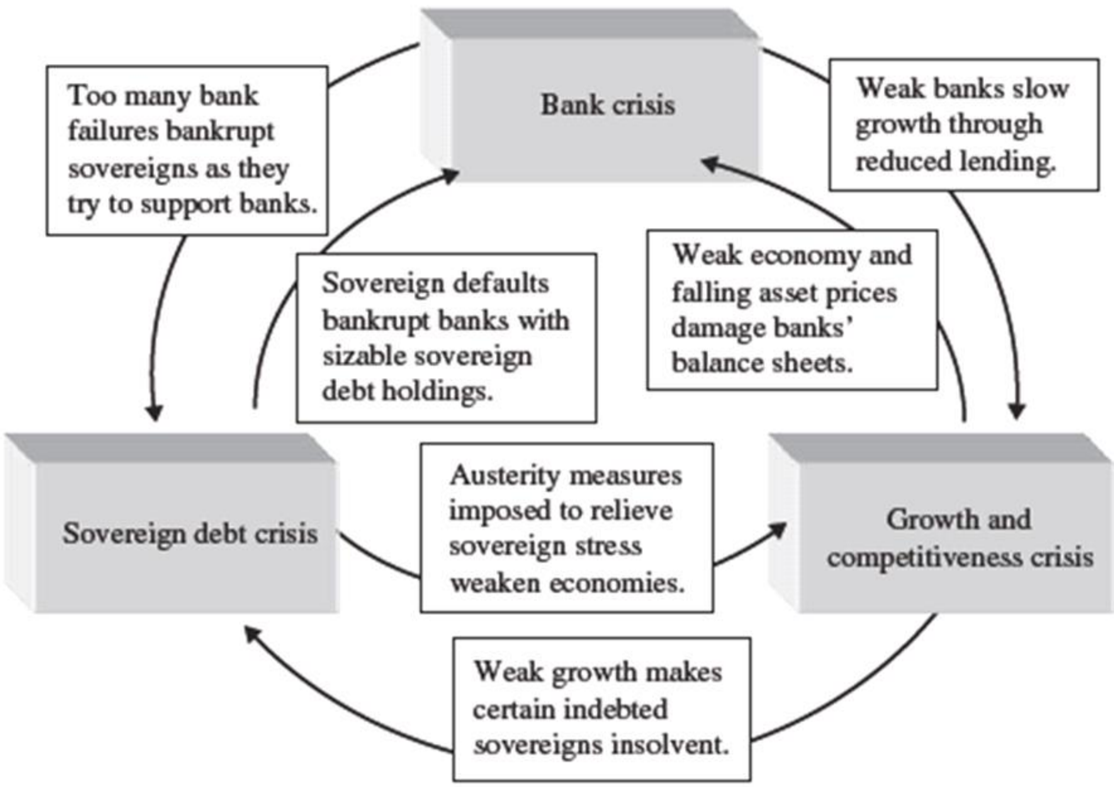
5.1 Analysis of the eurozone crisis

The eurozone crisis has three intertwined aspects. (Shambaugh, 2012). They are 1) fiscal and sovereign debt crisis, 2) bank crisis, and 3) growth and competitiveness crisis.

Diagram 1 Three aspects of the eurozone crisis



Source: Shambaugh (2012)

The first aspect (fiscal/sovereign debt crisis) came to the fore in spring 2010 after the revelation by the newly-inaugurated Greek socialist government that its predecessor regime had massaged fiscal balance figures in an apparent effort to become eligible to enter the eurozone, which led to financial markets' suspicions of the health of the Greek economy. The EU and the

International Monetary Fund (IMF) hastily arranged a huge bailout program for Greece whose benchmark 10-year government bond yield shot up, reflecting market worries. Greece was followed by Ireland in late 2010 and Portugal in 2011. The second bailout program for Greece was agreed in March 2012. The third bailout program was stitched up in July 2015.

The implementation of the bailout programs mirrored concerns among EU/eurozone policymakers that sovereign defaults, should they occur, may bankrupt banks with sizable sovereign debt holdings, starting a vicious circle.

It is noteworthy that of the first three rescued eurozone countries, Ireland "graduated" in mid-December, 2013, from its bailout regime and now fully rely on private markets to meet its financing needs rather than official loans. Irish 10-year government bond yield has dropped below 4 percent.

Greece remains the most problematic country in the list of those receiving rescue from the EU/IMF. Its first and second bailouts have provided the country with 246 billion euros of rescue financing, larger than Greek GDP.

But Greece continued to get bogged down in recession despite these bailout programs, with scant prospect of the country meeting its economic and fiscal reform targets dictated by the EU and the IMF during the three–year bailout program period that ran out in 2014. The IMF predicted that a hole of 4.4 billion euros would open up in late 2014.

In the circumstances, a financial/debt crisis flared up again in Greece in mid-2015 as the country was unable to honor its debt repayment to the IMF, which was due at the end of June 2015, prompting Greece to face the risk of a chaotic "Grexit." This was only averted after the Athens government led by Far Left Prime Minister Alexis Tsipras had agreed by July 13 to pay a high price for a third bailout of as much as 86 billion euros. It calls for Greece to meet strict terms, including new austerity and sweeping privatization measures. But many wonder if the deal will really help the country to stand on its own feet. Much depends on how resilient Greece is after the turmoil caused by the crisis.

It will take time for confidence to return to banks and depositors. The country faces a fresh dose of austerity, for example, through' the rise in VAT, which will raise 1% of GDP.

The IMF, which expects the total Greek debt to peak at almost 200% of GDP, believes that the country's burden could be made sustainable only through steps "that go far beyond what Europeans have been willing to consider so far. "

So the Greek debt problem will likely keep haunting its eurozone partners.

The second aspect of the crisis (bank crisis) hit Spain in 2012. As shown in Shambaugh's triangle diagram, weak banks slow growth through reduced lendings and it is also feared that too many bank failures bankrupt sovereigns as they try to support banks. As Rana and Bloomenhofer (2013) write, the banking crisis in the eurozone was first evident in Ireland but then spread throughout the region because of worries over sovereign solvencies, as governments had to bail out banks that had been ruined by the burst of housing bubbles. Hence the root causes of the European crisis were expansionary government policies in several countries, at least initially, and the weak financial regulations that led to overleveraging, on top of flaws in the design of the Economic and Monetary Union (EMU)..

The EU's banking union scheme is designed to cope with this banking aspect of the eurozone crisis. The scheme will be detailed in the next chapter.

The third aspect of the crisis (growth and competitiveness crisis) may be the most difficult to tackle because it may not be resolved through pouring more money or building institutions/systems.

As the Shambaugh's triangle diagram depicts, weak economy and falling asset prices damage banks' balance sheets. In the worst case scenario, weak growth makes certain indebted sovereigns insolvent and sovereign defaults bankrupt banks with sizable sovereign debt holdings in a vicious circle.

In the first place, weak economic growth leading to recession is a product of weak industrial competitiveness that result in many cases in the accumulation of current account deficits. To remedy such a situation, economic reform to strengthen competitiveness is needed.

Many eurozone periphery countries generally saw strong growth rates in the 2000s. Greek growth accelerated in the early 2000s, bolstered by spending for the 2004 Athens Olympic Games, while the Spanish growth has been reasonably high throughout the period. Ireland had also registered strong growth until it was hit by the Lehman shock in 2008. By contrast, German growth rates have remained mediocre throughout the 2000s, with the exception of the mini burst in the second half of the decade. The divergence of economic performances between Germany, the eurozone's largest economy, and periphery countries preceded the eurozone debt crisis. The crisis has its roots as much in the performance of Germany, as it does in the actions of peripheral countries. (*Lapavitsaset al.*, 2010)..

It can be also pointed out that in the background of the three aspects of the eurozone crisis lies overestimation of free markets (Mersch, 2011).

The financial crisis has put the legitimacy of absolute free financial markets into question. How financial markets have been assessing the creditworthiness of sovereigns within the euro area? Countries with weaker positions which introduced the euro could refinance themselves roughly at the same cost as the most solvent states. Elaborating on this point, spreads were very narrow, even between Greece and Germany. Financial markets then became irrationally pessimistic. Even wealthy states with sound economic fundamentals were having trouble in refinancing themselves at reasonable conditions.

In other words, it can be said financial markets are not always right in their reactions as they tend to move from one extreme to another at least in the short term. But over the medium- to long-term, they seem to have a self-corrective mechanism.

Meanwhile, in the spring of 2013, there was a lively debate on effects of a sovereign fiscal position on economic growth. It centered around an academic article published by Harvard University Professors Carmen Reinhart and Kenneth Rogoff in 2010 that had been widely interpreted as showing economic growth is likely to stagnate in a given country once the ratio of its government debt to gross domestic product exceeded a threshold of 90 percent(Reinhart and Rogoff, 2011). This paper, which the EU/IMF seem to have used as a theoretical basis on which they advocated stringent austerity policies to put a fiscal house in order in heavy-spending eurozone periphery countries that got mired in debt crisis. came to be disputed by scholars at the University of Massachusetts who had demonstrated and acknowledged that the two Harvard professors accidentally omitted some relevant data in forming their results due to a coding error (Summers, 2013). In addition, questions have also been raised with regard to how they weighted observations and which data they used.

Summers pointed out that many asserted the debate undermined the claims of austerity advocates around the world that deficits should be reduced quickly, with some having gone so far as to blame Profs Reinhart and Rogoff for the unemployment of millions. Others believe that even after review, the data support the view that deficit and debt burden reduction is important for most of the industrialized world, according to Summers (2013).

5.2 EU’s efforts to contain the euro crisis and prevent recurrence

Though the EU’s efforts to contain the eurozone crisis has often been criticized as “too late, too little,” it has slowly begun to bear fruit after ECB President Mario Draghi’s announcement of the central bank’s readiness to buy unlimited amounts of government bonds of a troubled eurozone country on condition that it agrees to clean up its fiscal house.

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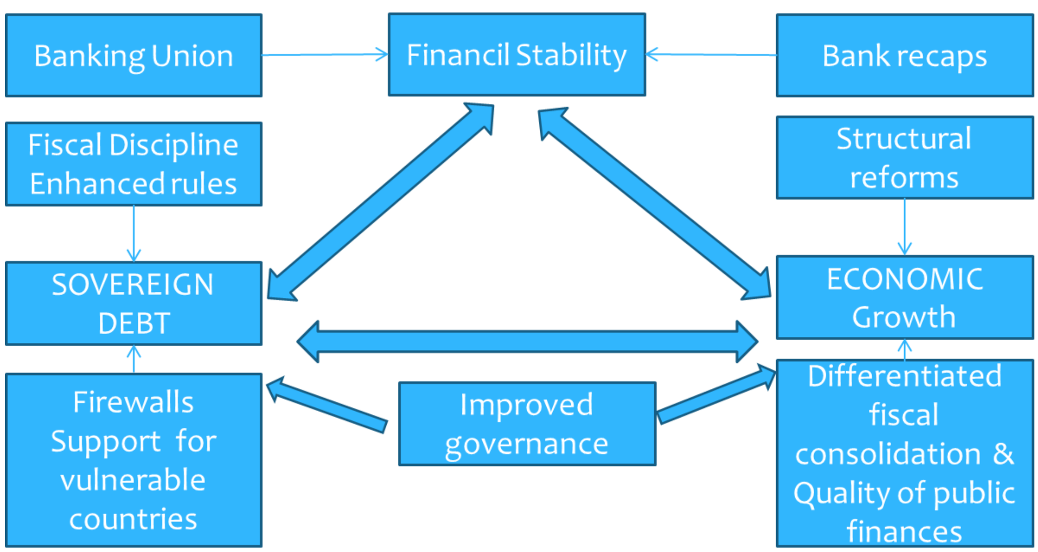
Peter Bexs, a senior European Commission official. showed the EU's three–pronged strategy to contain the eurozone crisis and prevent its recurrence in a clearly-written diagram he presented in a seminar sponsored by the EU delegation in Tokyo in late November 2012. It is based on EU President Van Rompuy taskforce's proposal and reverberates Shambaugh's analysis of the eurozone crisis.

The three pillars of Bexs' recipe are 1)measures to resolve sovereign debt crises through ensuring fiscal discipline and beefing up fiscal rules, building firewalls designed to support vulnerable countries and improved governance, 2) ensuring financial stability through establishing a banking union, and bank recapitalization, and 3) promoting economic growth through structural reforms and differentiated fiscal consolidation and improved public finances in terms of their quality. As shown in the diagram, the three measures are intertwined and thus are meant to strengthen each other..

Diagram 2 EU's efforts to contain the euro crisis



Source: Bexs (2012)

The taskforce led by President Herman Van Rompuy of the European Council, came up with the first version of its report titled "Towards a genuine economic and monetary union" in June 2012. The report first pointed out that the euro area is confronted with a rapidly evolving

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international environment characterized by the rise of large emerging economies and then emphasized the need for a more resilient and integrated EMU, saying it would buffer euro area countries against external economic shocks, preserve the European model of social cohesion and maintain Europe's influence at the global level.

The approach taken in the second Van Rompuy taskforce report （Van Rompuy, 2012） was divided into 1) the integrated financial framework, 2) integrated budgetary framework, and 3) integrated economic policy framework. The taskforce cited a single supervisory mechanism (SSM) for banks and a single resolution mechanism as its major elements. These two elements, along with a single bank deposit guarantee mechanism, should form a banking union covering the whole EU/eurozone. The credit resolution mechanism would be funded through an ex-ante risk-based levies on all banks directly participating in the SSM. It should include an appropriate and effective common backstop which could be possibly organized by means of an ESM (European Stablization Mechanism) credit line to the single resolution authority.

The second pillar (integrated budgetary framework) features stronger economic governance and an appropriate fiscal capacity for the euro area. The report says specific resources would have to be raised to finance both functions-promoting structural reforms and absorbing asymmetric shocks. It says these resources could take the form of national contributions, own resources, or a combination of both. In a longer term, it goes on to say, a key aspect of a future fiscal capacity, which would need to be examined carefully, would be its possible ability to borrow. A euro area fiscal capacity could indeed offer an appropriate basis for common debt issuance without resorting to the mutualization of sovereign debt. Two forms of common debt issuance are being discussed: longer-dated common eurobonds and shorter-dated eurobills that are similar to U.S. Treasury bills.

The German government seems to be vehemently opposed to the former as it is likely to lead to moral hazard on the part of troubled countries. On the other hand, the common issuance by euro area member states of short-term government debt with a maturity of up to 1 to 2 years would constitute a powerful tool against the present fragmentation of the robustness of government bonds, reducing the negative feedback loop between sovereign and banks, while limiting the morale hazard, argues the European Commission. .

Under the third pillar (integrated economic policy framework), the Van Rompuy report emphasizes that in the near term, it is essential to complete the Single Market as it provides a powerful tool to promote growth. It adds that there is a need for a thorough assessment of the performance of labor and product markets in the euro areas and that in the absence of exchange rate adjustments, a well functioning EMU requires efficient labor and product markets. This is essential to fight large scale unemployment, and to facilitate price and cost adjustments that are key for competitiveness and growth.

Referring to competitiveness, the report argues that it is important for the EU to be globally competitive and to avoid excessive divergences in competitiveness among EU members so that the EU can remain a highly attractive social market economy and to preserve the European Social models. The report says that the reforms introduced to the EU surveillance framework through the creation of the European Semester with country-specific recommendations and of a new Macroeonomic Imbalances Procedures with possible sanctions are a step in the right direction.

It should be also noted that the enhancement of competitiveness requires not just the reduction of labor costs but the promotion of innovations through a step-up in the development of high technologies.

Prior to the June 2013 European Council meeting, the Cabinet of the President of the European Council prepared a summary note on the State of Play of the consultations with members states and institutional actors related to plans incorporated in the "Toward a Genuine Economic and Monetary Union." The note says that the December 2012 Van Rompuy report shows a comprehensive and time-bound roadmap for the completion of the EMU and that the roadmap rested on four building blocks: an integrated financial framework (the "banking union"); an integrated fiscal framework; and integrated framework for economic policy; and the measures necessary to ensure democratic legitimacy and accountability.

The democratic legitimacy and accountability measures underpin smooth building and implementation of the preceding three frameworks.

The note also points out the importance of the social dimension of the EMU. It says the eurozone crisis has shown that lasting financial and economic divergences, if not corrected in due time, may threaten the financial stability of the euro area as a whole. It quickly adds that yet increasing unemployment, growing poverty and exclusion are also harmful to the EU's economic potential and social cohesion. The note also says that the promotion of a high level of employment, the guarantee of adequate social protection, the fight against social exclusion, and a high level of education, training and protection of human health are an integral part of Europe's global competitive advantages.

Second, the note stresses the importance of ex-ante coordination of national reforms in the all policy areas that are essential for functioning of the EMU, such as labor, goods and services markets, public sector, tax, education, and pension.

The Conclusions of the June 2013 European Council says that in the short term, the key priority is to complete the banking union. The banking union is considered as a key to ensure financial stability, reducing financial fragmentation and restoring normal lending to the economy. The European Council believes it is imperative to break the vicious circle between banks and sovereigns .

The eurozone crisis had largely abated after September 2012 when ECB President Draghi announced the central bank's intention to buy unlimited amounts of troubled eurozone countries' government bonds under the OMT (outright monetary transactions) operation in a resolute bid to defend the single currency.

As mentioned above, the new Greek debt crisis erupted in the middle of 2015, which led the country to the brink of a chaotic "Grexit."

Lots of potential risk factors remain, including slow progress in the bailed-out countries' reform, especially in Greece, precarious political situation with a razor-thin parliamentary majority in such countries as Italy and Greece, and near-record unemployment rates in many eurozone countries.

The EU for its part has put in great efforts to end once and for all the eurozone crisis and prevent a recurrence of a similar one. It has made no small achievements so far, with agreements on a variety of fiscal consolidation and imbalance correcting measures, and the planned inauguration of a single banking supervisory mechanism under the nascent banking union. But the EU still has a long way to go.

5. Need to engage China to create more robust financial governance system

China's rise to the second largest economic power, eclipsed only by the United States, in 2009 also testifies to its growing importance in global finance.

But the Chinese economy, under its one-party (Communist Party) rule, seems fraught with fragilities. This leads to the question of "Is the next Lehman shock in making in China?" In the background are such factors as property bubbles and fast economic growth. Besides, China's financial system has few international connections. How Beijing will behave when troubles strike? Its response is hard to predict. But there are some assuaging factors, too. Among them are:

1) China is a big net saver.

2) Its banking system is largely deposit oriented.

3) Beijing has the fiscal capacity to underwrite trouble loans.

Now this paper turns to the need to engage China.

As part of the IMF reform, voting rights have been expanded for China and other emerging countries. Even if China is joined by four other BRICS countries (Russia, India, Brazil and South Africa), their combined votes at the IMF stands at around 15%. The United States owns 17.40% of votes at the IMF and can exercise a veto power. The BRICS countries' voting powers are not proportionate to their GDP sizes. China and three other BRICs countries account for about a quarter of the global GDP.

The following table shows shares of GDP in the world and new IMF voting rights (%)

Table 1 Major countries' shares of GDP and IMF voting rights

	Share of global GDP	**Share of IMF voting rights**
US	19.2	17.4
China	16.1	6.39
India	6.0	2.75
Russia	2.9	2.71
Brazil	2.8	2.32
South Africa	0.7	0.8

China's interest in the IMF and the World Bank, always half-hearted is waning. The BRICS have agreed at their summit in Brazil in July 2014 signed off on the creation of the group's first real institution, a development bank as well as a $100billion joint currency reserve fund aimed at helping to fight financial crises. The BRICS bank could become a welcome alternative to the bureaucratic and highly conditional lending of the IMF and the World Bank. The biggest

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rationale for them to act together is how little global economic governance has advanced (FT July 17, 2014).

In the circumstances, suppose the West collaborate with China to liberalize the latter's capital account, China's financial markets would become less distorted. while the emergence of the yuan as a global reserve currency would ease Western fears about their currencies' overvaluation (*Economist*).

On the other hand, there is a pessimistic scenario.

The creation of the BRICS bank is feared to lead to the fragmentation of world economic governance, ushering in multiple centers of power competing for influence. (*FT*), The BRICS are not as united as they appear and the new institutions they are setting up face formidable operational challenges (ibid.).

The test of the new BRICS institutions will come when one of the members runs into trouble and demands a big loan (ibid.)

Then there is this ongoing China-led scheme to establish the Asian Infrastructure Investment Bank, a regional bank which is likely to be in rivalry with the World Bank and the Asian Development Bank.

Global opinion seemed to be divided when China announced the AIIB plan.

For the gloomy mangers, many of whom reside in the U.S. Administration and Congress, the creation of the AIIB represents a power-grabbing by Beijing, which can be regarded as the economic counterpart to the Chinese Navy throwing its weight to around the South China Sea (*FT*).

For optimistic souls, the AIIB represents a move towards transparency by China, which has long lent out its vast foreign exchange reserves for development projects unilaterally and without transparency (ibid.).

If China wants legitimacy for its lending by inviting in other countries, it should accept the norms of transparency that they bring with them (ibid.)

The United States and Japan are the only major developed countries that have not announced intentions to join the AIIB, being skeptical of the degree of transparency of its management and lending practices.

6. Elements of a new economic order

First, the author observes that there are two institutional elements of global financial governance: G20 and the Financial Stability Board, which is a technical group dealing with regulation.

But the problem of inclusion persists (Germain, 2001), both at the country level and the level of citizens. The former was explained in chapter 5.

As for the latter, revolt has been spreading in the international system against a global economy characterized by open markets, unrestricted capital flows, and the activities of multinational firms as epitomized by "Occupy the Wall Street" movements.

To remedy the situation, a new, more just and sustainable international economic order should include such elements: mechanisms to combat poverty, to solve environmental crises, and promote human development in areas including health, education and housing.

7. Conclusions

Crises have shaped global finance as shown in the aftermaths of the five disasters mentioned above.

In the post World War IIconext, Bretton Woods institutions have survived, but the problem of "inclusion" has emerged, namely the problem concerning the need to engage China and other emerging nations in global finance.

In more recent times, lessons from the Lehman shock have not been learned. Since 2008, there had been a mass of new rules from America's Dod-Frank law to transaction taxes in Europe. Though some steps to boost banks' capital and liquidity do make finance more self-reliant.

Meanwhile, there are high expectations about the emerging banking union in Europe following the eurozone crisis. It could enhance financial governance at least in the eurozone.

The author pointed to two new institutions that could boost global financial governance: G20 and the Financial Stability Board.

To back up global financial governance, there is a need for growth strategies as well as a new, more just and sustainable world economic order that takes into account poverty, environment and human development issues.

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All in all, in modern finance debt-fueled housing goes wild, while investment in machines and patents runs dry. All this dulls growth.

Finally, it may be too early to tell whether robust global financial governance is still possible, but with the assertion of economic powers by BRICS countries as exemplified by the creation of a new international development bank, global finance is starting to get bipolarized in some sense, making unified and coherent governance more difficult.

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