

Arminio Fraga: Bretton Woods at 75

The framework of multilateral economic cooperation established in 1944 is under serious strain, if not broken. Nevertheless, the Bretton Woods institutions, together with more recently established international and regional forums, still have a meaningful long-term role to play in global economic governance, writes **Arminio Fraga**



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Global governance explained

The 1944 Bretton Woods conference established a multilateral framework for global cooperation on macroeconomic stability, trade, and development that has endured – despite inevitable disruptions and adjustments – for 75 years. We should celebrate and praise these achievements. And, although this system of global economic governance is now under serious strain, the Bretton Woods institutions, together with more recently established international and regional forums, will still have a meaningful long-term role to play.

At the macro level, Bretton Woods was based on fixed but adjustable exchange rates, and relied on the newly created International Monetary Fund to monitor the consistency of national policies and provide financial support to countries facing external shocks. The new World Bank (which began as the International Bank for Reconstruction and Development) provided support and advice on long-term investment projects for development and reconstruction. And another postwar

institution, the General Agreement on Tariffs and Trade – expanded and reestablished as the World Trade Organization (WTO) in 1995 – provided a framework for advancing free trade, based on multilateral rules and dispute mechanisms.

This global arrangement allowed plenty of room for different national and regional approaches, as long as policies did not lead to recurring balance-of-payments and inflation crises. Successful countries were able to accumulate more capital, especially human, and build institutions that made their gains more permanent. In many ways, the national strategies that paid off were convergence bets – ones that aimed to narrow productivity gaps with more advanced economies.

Alongside the economic advances, many commentators saw clear signs of political convergence toward more liberal democratic regimes, culminating in the fall of the Berlin Wall and the collapse of the Soviet Union. The American political scientist Francis Fukuyama summarized this narrative with his famous “end of history” thesis.

Challenges and crises

Over time, the Bretton Woods regime faced numerous challenges and crises. The move away from explicit exchange-rate parities to a system of more flexible currencies in the early 1970s marked the end of the original postwar monetary framework, but formal and informal inflation targeting subsequently re-anchored the system.

True, many developing countries suffered far greater inflation and balance-of-payments problems than more mature economies, but efforts to restructure their international debts and deal with high or hyperinflation were quite successful. The World Bank and regional development banks adapted to a world of ever greater capital needs by playing a more informational and catalytic role in areas such as infrastructure and institution-building. And despite slow or no progress at the WTO level, many bilateral and regional trade and investment arrangements were put in place.

Today, however, global economic coordination has become more difficult, if not outright impossible in some areas. On trade, despite the proliferation of regional arrangements, there has been no meaningful multilateral progress since the Uruguay Round in 1994. On climate change and the environment – a contemporary existential imperative – recent negotiations have yielded limited results. Global public goods remain undersupplied in key areas such as security, migration, and global health. And debt continues to grow in many countries, often surpassing levels reached in the run-up to the 2008 global financial crisis.

Even some of the regional trade achievements of the past quarter-century are now vulnerable, such as the European Union’s single market (assuming Brexit happens), the recently replaced North American Free Trade Agreement, Latin America’s Mercosur bloc, and the Trans-Pacific Partnership.

In parallel with these economic challenges, there is widespread popular frustration at most countries’ inability to deal with the negative social implications of the current global development model.

Evolving arrangement

In this context, it is no surprise that newer forums such as the G7, G20, and the Financial Stability Board have partly replaced the formal Bretton Woods institutions. Because decisions taken in

international institutions often carry the force of law, many countries increasingly prefer to meet in forums that issue mostly non-binding statements (a point often made by the late Tommaso Padoa-Schioppa, a former European Central Bank board member and Italian finance minister).

Although not as strong as the original Bretton Woods design, this evolving arrangement may indicate that the global system for economic governance is flexible and can adapt to changing circumstances. But, for the larger countries or blocs such as the United States, the European Union, China, and Japan, the formal Bretton Woods system is no longer central to macroeconomic stability, trade, or finance.

World in transition

So, what can we say about Bretton Woods in a world in transition?

- First, with the US less dominant and less willing to provide global economic and financial leadership, systemic instability is likely to increase. As the American economic historian Charles Kindleberger famously warned, this typically occurs in transitional moments when a global hegemon is absent. Some signs of this are already visible in trade and regional tensions, growing leverage, and rising nationalism.
- Second, “Bretton Woods” should now be seen to include not only the original institutions, but also more recently established global forums and regional arrangements. These mechanisms of cooperation constitute a realistic practical response to current challenges.
- Third, one must ask whether developing countries will continue trying to converge with more advanced economies, and whether the expanded Bretton Woods family of institutions can remain meaningful stewards of global progress. My answers tend toward yes to both, if one takes a long-term view. Developing countries will aim to emulate the earlier successes of the Asian Tigers and Eastern Europe. And countries will prefer dialogue and cooperation to the failures of those such as Venezuela and North Korea that opted out of the global system.
- Lastly, this hopeful vision may now be under threat from the disturbing shift toward illiberal and populist political regimes around the world. But history shows that liberal politics and economic policies have undoubtedly delivered more progress and peace than any other system.

Seventy-five years ago, economic policymakers gathered at Bretton Woods to create a new financial order for the postwar world. Today, their successors can still draw on some of these achievements in designing a global economic governance system for the twenty-first century.

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