A multipolar IMS: likelihood, desirability, transition

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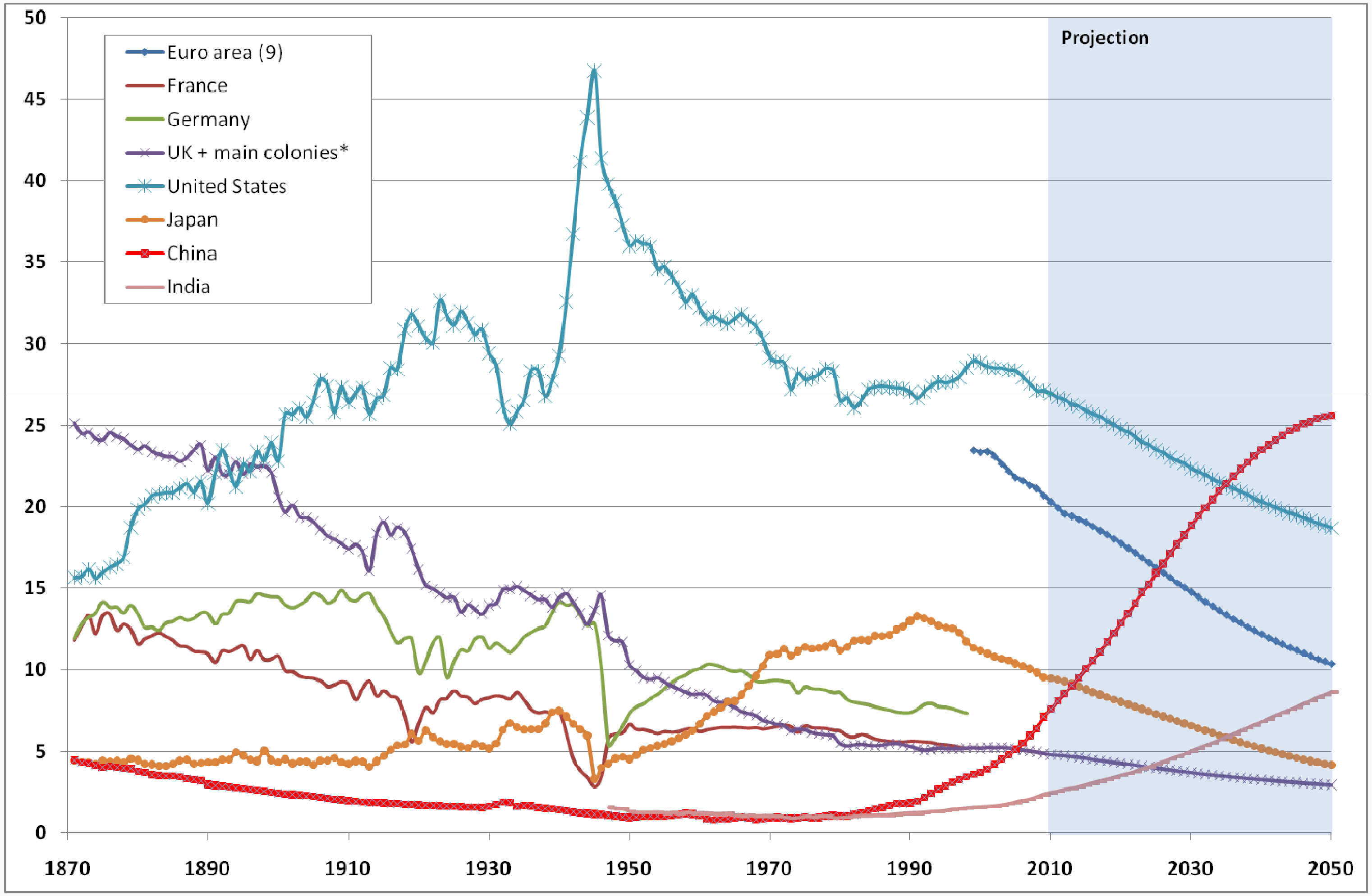
1. Likelihood
An increasingly multipolar world

Percentage shares of selected countries and areas in world GDP, 1870-2050
(At 2005 exchange rates and prices)



Sources: Angus Maddison's historical statistics and CEPII projections.
* Australia (up to 1900), New Zealand (up to 1939), India (up to 1946). Canada is not included as it was already granted significant autonomy in 1867.

The potential for a multi-currency system

	US dollar	Euro	Renminbi
Size	27% of world GDP, decreasing	20% of world GDP, decreasing (but potential for enlargement)	7.6% of world GDP, increasing
Financial markets and openness	Unrivalled liquidity and depth, full capital mobility	Second after the US, but bond markets remain fragmented in the absence of unified Eurobonds. Full capital mobility	Underdeveloped markets and restricted capital mobility
Legal system	Strong	Strong	Weak
Budgetary and monetary policy	Increasing concerns over the sustainability of budgetary policy and the risks of debt monetisation	Strong monetary record and institutional independence. Concerns over solvency of some individual state borrowers	Strong fiscal position. Good monetary policy track record but at risk, in part because of currency peg
Ability /willingness of policy system to respond to unexpected shocks, LLR* function	Strong	Strong for central bank but broader capacity limited by institutional arrangements	Strong
Stance towards international currency role	Incumbent	Officially neutral. Unilateral euroisation by non-member countries actively discouraged	Support for early steps of RMB internationalisation
Political cohesion and geopolitical power	Strong	Limited by political fragmentation	Strong and in ascendance

Note: * Lender of Last Resort.

2. Desirability
Main flaws of the current regime

- **Lack of automatic adjustment**
  - Asymmetric adjustment falling mostly on non-US deficit countries
  - Imperfect capital mobility and exchange-rate flexibility, hence asymmetric adjustment
- **Uncertainties surrounding emergency liquidity provision**
  - Bilateral: major role in the crisis, but discretionary
  - Regional: developing but still limited (Europe, East Asia)
  - Multilateral: in progress, but lack of trust and fear of stigma rightly or wrongly remain, which justifies (or serves as pretext for) self-insurance through reserve accumulation
- **No clear global anchor**
  - A more relevant issue in the post-Great Moderation world
- **Dollar-centered IMS increasingly at odds with the global economy**
  - Change in global economic power towards emerging economies
  - Inadequacy of US monetary policy for fixers
  - New Triffin dilemma

Monetary implications of power shift with unchanged IMS

- **Flaws to become more severe as economic centre of gravity moves**
  - Who will provide global anchor?
  - How large the world demand for US assets?
  - How willing the US to play hegemonic stability role?
  - How acute the disputes on exchange rates?
  - How effective coordination ?
- **Increasing risks to the stability of the system**
  - Risk of mismatch between US policy and dollar role leading to abrupt diversification away from USD assets

Implications of a multipolar IMS

1. **Efficiency**
   - Limited loss in terms of transaction costs
   - More market-driven exchange rates, less long-lasting misalignments
   - Less reserve accumulation, more scope for diversification
2. **Stability**
   - Market discipline versus short-term volatility
   - United States no longer able/willing to play hegemonic stability
3. **Equity**
   - Shared privileges and duties
   - More symmetry of adjustments and stakes

3. Transition time frame

	2011	2015	2020-25
Risks	Collapse of the €	Collapse of the $	New imbalances
G20 priorities	Global demand & liquidity	Global imbalances	Stability
IMS	Status quo+ (credit lines)	More ER flexibility and K^{al} mobility in China SDR+ Eurobond	Multipolar IMS G5

The RMB in the SDR?

- **Cannes summit (Nov. 2011):**
  - **“**We look forward to reviewing the composition of the SDR basket **in 2015, and earlier if warranted**, as currencies meet the criteria, and call for further analytical work of the IMF in this regard, including on potential evolution”
- **Feasibility**
  - RMB not “freely usable”
  - But do we need more “freely usable” currencies?
  - Flexibility maybe more important than free usability
- **Desirability/timing**
  - Present composition: only currencies of advanced economies, hence risk of a depreciation trend of SDR against emerging currencies
  - With RMB:
    - More stability
    - Incentive for the PBoC to provide dollars in exchange of SDR on a voluntary basis
    - Incentive for emerging countries to adopt pegs on the SDR
    - Attractiveness of SDR even before free usability of RMB (SDR as shadow RMB)

The RMB in the SDR: do not wait too long

- RMB could already 10% of the basket
- Risk of a discontinuity when the RMB is eventually included

Table 1 – Composition of the SDR per year of review,* with and without RMB, in percent

		2000	2010	2020	2030	2040	2050
USD	Without RMB	45.0	41.9	41.5	41.1	41,0	40.7
	With RMB	44.0	37.6	37.9	36.7	35.7	35,0
EUR	Without RMB	29.0	37.4	38.1	37.9	37.5	37.3
	With RMB	28.0	33.4	30.9	27.8	25.1	23.3
GBP	Without RMB	11.0	11.3	10.4	10.3	10.2	10.2
	With RMB	10.0	10.1	8.3	7.3	6.5	6,0
JPY	Without RMB	15.0	9.4	10,0	10.7	11.3	11.7
	With RMB	14.0	8.4	7.5	6.9	6.3	5.8
CHN	Without RMB	-	-	-	-	-	-
	With RMB	4.0	10.5	15.5	21.3	26.4	29.9

* Weights apply for five years starting the year following the year of the review.
Source: IMF and authors' calculations.

Source: Bénassy-Quéré and Capelle (2011).