Wanted: a new financial order

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BRUSSELS — A week ago, French President Nicolas Sarkozy and German Chancellor Angela Merkel found themselves strolling together through the cobble-stoned streets of Colombey-les-Deux-Églises, a tiny village in the northeast of France, where they were attending a war-memorial ceremony.

The town is known as a place where French leaders, from the time of Charles de Gaulle, have gone to escape the world and restore their energy. There was much retreating and restoring to be done last Saturday: The previous day, their finance ministers had rushed home early from a Washington crisis meeting after stock markets had crashed dramatically and expensive national schemes to restore the credit system had failed.

None of the patchwork of plans appeared to work and the world economy was threatening to seize up. A few hours earlier, the head of the International Monetary Fund — a Frenchman — had declared that the world financial system was "on the brink of systemic meltdown." Both leaders had been on the phone with British Prime Minister Gordon Brown, and they had agreed to follow his plan for governments to purchase major stakes in their countries' failing banks, at huge expense. With that done, anything seemed possible.

It was during their stroll, and over lunch afterward, that these two often-feuding leaders arrived at another conclusion: Nothing would be truly fixed, they believed, until there was a new world financial system in place, a new economic watchdog supervising the world's economies.

A picture from the U.S. National Archives released by the International Monetary Fund show U.S. Secretary of the Treasury Henry Morgenthau welcoming delegates during the opening meeting of the Bretton Woods Conference. *(U.S. National Archives/AFP/Getty Images)*

That was a view that had been pushed strongly by Mr. Brown, in a memo that he had begun circulating among associates and leaders, and it agreed, on the surface, with something similar to what Mr. Sarkozy had been saying for weeks: That this was an unprecedented global crisis, beyond the scope or powers of any national government.

The next step, they agreed, would have to involve the whole world, and would require rewriting the rulebook of global capitalism.

With that lunch, Europe had reached a consensus, at least superficially, on a solution that had not been attempted in 64 years: a major global meeting that would attempt to redesign the world-finance system. It was an acknowledgment, at a high level, that with the current crisis, the entire postwar economic system may have come to an end. What comes next will be a matter of heated disagreement.

By Tuesday morning, the Americans were on board, at least as far as attending the proposed meeting — expected to be held in New York shortly after the Nov. 4 presidential election. Prime Minister Stephen Harper, fresh from his re-election, said Friday he also supports holding the meeting. All the G8 industrialized nations have agreed to attend, at least on paper, and it is expected that China, Brazil and India will take part.

While there's no consensus on what the new financial order should be and there are signs of deeply divergent views, these countries appear at least willing to talk about a new international order at a meeting the three European leaders are calling Bretton Woods II, after the 1944 meeting that started it all.

"Merkel became convinced at Colombey that Brown and Sarkozy were correct that the whole postwar system of finance does not work any more, and something new will have to take its place," said a European Union official involved with the talks.

Saturday morning, the Europeans will try to take Washington a step further. Leaving early from the Montreal summit with the Canadian government, Mr. Sarkozy and European Union Commission president José Manuel Barroso will fly to Camp David to sit down with President George W. Bush and try to persuade him to support Mr. Brown's proposals to create a new set of international institutions.

What they will be trying to sell is a seven-page document that Mr. Brown first made public on Wednesday morning. It proposes a set of organizations — a "new international financial architecture for the global age" — that will monitor risks in the financial system and provide an early-warning system; determine global standards of regulation; supervise international corporations in their cross-border activities, protect markets from excessive activities of speculators; stamp out major conflicts of interest and set standards for pay and bonuses; internationalize accounting standards, and provide transparency in complex financial transactions.

Given these sizable goals, the encounter with Mr. Bush may be the Europeans' least victorious moment: Aides to Mr. Bush said last night that he is not interested in a new international organization, would prefer to have debt and finance overseen by national bodies, and does not even want to fix a date for the meeting. Other Americans, notably Treasury Secretary Henry Paulson, are said to be more receptive: After all, it was Gordon Brown's bank-buying scheme that tamed the market crash after Mr. Paulson adopted it in the U.S. on Tuesday, at a cost of $250-billion.

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"There's generally agreement that the rules used worldwide in the banking and financial system have probably to be changed," says Philippe Waechter, a world-finance expert who is head of research for the French firm Natixis Asset Management.

What exactly has to be changed, though, is a hugely contentious matter.

In 1944, while tens of thousands of soldiers were still dying in Europe's forests and villages, another era came to an end. Since the beginning of the First World War, the world's economy, which previously had been fluid, open and international, had become divided and segregated along national lines. This nationalism, protectionism and currency isolation had deepened with the 1930s Depression, and leaders of Britain and the United States feared that this would prove economically fatal in the postwar years.

John Maynard Keynes, the British economist, called for a major meeting of world leaders — to be held a few days after the D-Day landings — at the Mount Washington resort hotel in the mountain ski resort of Bretton Woods, N.H. The gathering was known as the United Nations Monetary and Financial Conference, although the United Nations did not yet exist.

Winston Churchill, Franklin Roosevelt, Joseph Stalin and Mr. Keynes, along with 700 officials from 44 nations, gathered in Atlantic City, N.J. on June 15 and then took the train to New Hampshire and met for 22 days — a far more leisurely pace than anything that will be held this year.

They were there to address a burning problem raised by Mr. Keynes: If, when the war ended, European recovery and rebuilding was to happen in any meaningful way, there would have to be free flows of capital and investment between borders, and currencies would have to be able to be exchanged for one another. No longer could nations act on their own; they would have to be sending capital across borders, often large amounts of it.

Over cocktails and steak dinners, the leaders built the architecture of the modern financial world: the International Monetary Fund, which provides loans to rescue countries in financial trouble; the body known as the World Bank, which finances the rebuilding of troubled economies, and the institution that became the World Trade Organization, designed to open borders and break down trade barriers.

Bretton Woods began a six-decade process of the de-politicization of money: In ever more dramatic ways, government and finance became separate spheres, and banking became a self-contained, increasingly unregulated world of its own. A flood of savings from the developing world provided banks with huge pools of money they could use to devise new profit-making instruments, free from interference.

Until this week, that is, when government and money came crashing back into one another. Suddenly, governments are the major providers of loans, and the major shareholders in banks, and the ability to keep the money flowing is beyond the authority of any one country. The idea that central banks can quietly stick to keeping inflation at bay is gone. Once again, we are aiming for the prevention of catastrophes.

On Monday, Mr. Brown arrived at a meeting of the 15 countries that have the euro as their currency and laid out, behind closed doors, that vague but sweeping set of proposals he would make public two days later.

"We now have global financial markets, global corporations, global financial flows," he told them. "But what we do not have is anything other than national and regional regulation and supervision. We need a global way of supervising our financial system."

The idea became surprisingly popular in Brussels on that day, partly because Mr. Brown's vagueness turned his seven-page plan into something of a Rorschach test on which could be projected each country's economic fantasies. Italian President Silvio Berlusconi talked about a world without the dollar, where the euro might become the reserve currency.

The otherwise conservative Mr. Sarkozy declared in a grandiose speech that "we need to found a new capitalism, based on values that put finance at the service of companies and citizens, and not the reverse." Such lines play very well in France, but are not likely to win any high-fives from Mr. Bush this morning in Washington.

Before a meeting date could even be set, the leaders squabbled over who had invented the idea. Mr. Sarkozy, through his aides, make it known that he had been proposing since Sept. 23 that a new global regulatory system be built.

Mr. Brown, in turn, had his aides point out that in January of 2007 he had argued that international finance regulation was "urgently in need of modernization and reform."

All of this sounded a bit rich to a community that had watched these European leaders, notably Mr. Brown as Britain's finance minister in the late 1990s, participate in a deregulation and neglect of the financial system that had allowed the complex network of mortgage-backed debt instruments to spiral out of control and destroy the debt-burdened banking system.