

# Comment

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A good article like Volcker's on "Globalization Stability and the Financial Markets" inevitably raises as many problems as it solves.

The recent crisis hitting countries in Asia helps bring the advantages and drawbacks of globalization into perspective, while also prompting a question: just how many central banks are there in a global world?

In any analysis of financial market activities, the first point to settle is the contribution they make to growth in income, and thus in the general well-being. And this in turn means ascertaining whether the markets are indeed stable and efficient, or whether their characteristically changeable behaviour actually contradicts their presumed efficiency.

Volcker's view – hardly surprisingly – is very close to that of the central bankers. It is not true that the financial markets always follow an equilibrium path rationally reflecting the underlying 'fundamentals', but neither is it true that the financial markets fluctuate without any anchor, entirely at the mercy of 'ignorant' speculators.

The view expressed here rightly takes the middle way: growing markets have a positive effect on the growth of the economy, and manifestly so, for if they did not they would eventually disappear.

Moreover, the instability they show is systemic, tending to recur: the Asian crisis is only the most recent but by no means the last of a series of financial crises regularly occurring in various parts of the world over the last twenty years. The instability factor means that corrective mechanisms are necessary. And all the more necessary, I may add, when the 'patience' of the direct investors, or in other

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words capital invested over the long term, gives way to the 'greed' of portfolio managers, or very short-term investments. As markets become increasingly liquid they lose the long-period perspective so needed to meet these cases.

The far-sighted view is to be seen as emerging from *policy* correctives, or in other words afforded by leaders responsible for anticipating and guiding the markets, avoiding the 'moral hazard' problem arising when the market awaits a lender of last resort, who then fails to match up to the task he has undertaken (or which has perhaps only implicitly been expected of him).

In actual fact, the major financial crises of the last twenty years came about through shortcomings of the *regional markets*, resting on real and financial structures that developed internal contradictions. Cases in point are South America in the early Eighties and, again, the present crisis in Asia. In the former case it was American monetary policy and appreciation of the dollar that sparked off the crisis, in the latter Japanese malaise and depreciation of the yen. Both cases show similar patterns: stock market and exchange crash, financial straits, bankruptcy looming up for the weakest of the brokers. A point to stress here is that in either case it is the various central banks that show the most striking shortcomings. Actually, there is something absurd about speaking of central banks in the plural, as if an integrated market could have manifold leaders. The market crisis now unfolding before us has its origins in the insistence those countries showed in preserving fixed exchange rates with the US dollar a little too long. Fixed exchange rates do in fact promote integration, but they do call for far greater responsibility.

We have seen as much in Europe, among countries somewhat more mature and less exposed to speculation: fixed exchange rates lead to integration but need coordination, both to increasing degrees. One inevitable result of globalization is the dwindling number of truly central banks. The term may be applied to a bank that, in the face of rapidly growing markets, is able to prevent or – if too late for that – cure the ills of financial instability. A bank is 'central' if it can match up to the market it is responsible for, ensuring liquidity when it is threatened by crisis or solvency when the crisis is one of confidence.

All too many central banks show a dangerously illusory façade of stability, proving inadequate precisely when the real need arises. In his paper Volcker expresses justified concern that stability has got left out of the construction of the global market. I might add, paraphrasing a slogan much in vogue in Europe, "One market, one central bank".