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The Global Crisis and the Future of the Dollar: Toward Bretton Woods III?

by

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ABSTRACT

This paper investigates the U.S. dollar's role as the international currency of choice as a key contributing factor in critical global developments that led to the crisis of 2007–09, and considers the future role of the dollar as the global economy emerges from that crisis. It is argued that the dollar is likely to retain its hegemonic status for a few more decades, but that U.S. spending powered by public rather than private debt would provide a more sustainable motor for global growth. In the process, the "Bretton Woods II" regime depicted by Dooley, Folkerts-Landau, and Garber (2003) as sustainable despite featuring persistent U.S. current account deficits may turn into a "Bretton Woods III" regime that sees U.S. fiscal policy and public debt as "minding the store" in maintaining U.S. and global growth.

Keywords: Reserve Currency; Global Monetary Order; Global Financial Crisis

JEL Classifications: E12, E61, E62, F02, F33

I. INTRODUCTION

Back in 2007 we used to refer to the current crisis as the "U.S. subprime crisis," but while it was the area where troubles first emerged, the subprime mortgage sector turned out to be only the tip of the iceberg. Today, the Lehman crisis of mid-September 2008 is still widely seen as the critical blunder that pushed the U.S. and world economies off the cliff. Yet the Lehman bust may have been no more than just the trigger of an implosion of underlying financial structures that had built-up to reach a cracking point many years before.

In assessing the roots of the ongoing crisis, and also the prospects for a sustained recovery, due account has to be taken of the central role of the U.S. dollar in the world economy. The world monetary and financial order—with the U.S. dollar as its hub—conditioned and induced particular macroeconomic policies in the rest of the world and in the United States, policies that led to the buildup of global (and domestic) imbalances and underlying international (and domestic) credit structures. The Lehman crisis was a key event in their malign unwinding, and it prompted important policy responses around the world, too, but certain underlying dynamics in the global economy may not change for as long as the dollar retains its special global status. Therefore, in weighing domestic policy options at the current juncture, it is important also to consider the future role of the dollar in an evolving and increasingly integrated world economy.

II. GLOBALIZATION UNDER A DOLLAR-CENTERED GLOBAL MONETARY AND FINANCIAL ORDER

The U.S. economy has become more "open" in terms of trade and investment flows, with correspondingly heightened vulnerabilities to external events that global linkages and interdependencies inevitably bring with them—a tendency called globalization that the United States shares more or less equally with much of the rest of the world. Even more important, the United States is not only unique in the world, but also uniquely important for standing at the top of the international pecking order of currency and finance. Because the world monetary order is dollar-centered, U.S. financial institutions have long enjoyed a supreme position in global finance. It is thus noteworthy that this order is asymmetric in that one player is more equal than

everyone else—a special status that comes along with both special benefits and responsibilities. The behavior of the country at the hub of the order is of the greatest systemic importance, but remains conditioned by other players' conduct as well.

In much of the rest of the world, rising globalization under the asymmetric dollar-centered order has induced governments to pursue defensive macroeconomic policies. The world financial system has become increasingly globalized in its reach and operations. However, regulation and supervision of financial institutions engaged in cross-border activities have remained predominantly national. This mismatch creates a highly unsafe environment, especially for countries further down the currency hierarchy. The resulting loss in economic sovereignty through global integration has put a premium on policies that help preserve whatever little control and room to maneuver individual countries may have left. In general, seeking protection has taken the form of maintaining a competitive exchange rate vis-à-vis the U.S. dollar, running up current account surpluses, and accumulating soaring foreign exchange reserves—predominantly denominated in U.S. dollars—as self-insurance (Bibow 2008 and 2008–09).

A common tendency among countries that pursue policies of this kind has important systemic implications; if everybody pushes exports and aspires to accumulate dollar reserves, strong deflationary forces arise in the system as a whole. In fact, under a 1930s gold standard system that was characterized by a given amount of gold reserves available for precautionary hoarding, such rising systemic pressures would have led to a severe tightening of financial conditions, bank runs, and, ultimately, deflation and financial meltdown. While individual countries could chose to get off gold or depreciate their currency relative to gold, the gold standard order as a whole lacked a mechanism to offset systemic deflationary pressures by augmenting the system's reserves correspondingly. That factor contributed to the severity of the Great Depression (Keynes 1931; Bernanke and James 1991; Eichengreen 1992).

Today's world monetary order is not a gold standard, but a U.S. dollar standard. The amount of U.S. dollars available to be held as reserves by other countries is not physically constrained as in the case of gold, but generally depends on the evolution of the U.S. balance of payments over time and on U.S. macroeconomic policy decisions at critical junctures in particular. Systemic deflationary forces can develop in this system too, but they can more easily be offset by a flexible U.S. macroeconomic policy response, so the ultimate outcome of the current crisis may be less horrific than the Great Depression.

The country issuing the system's key reserve currency has a special responsibility under crisis conditions. Under more normal conditions, too, meeting the key reserve currency's systemic role may also come about quite naturally and in full accordance with the national interest. The point is that a general desire among the rest of the world to export to the United States and accumulate dollar reserves produces strong deflationary forces in the domestic economy of the reserve currency issuer. Weakness in U.S. labor markets and downward pressures on wages and prices in general arise. These market pressures will normally convince U.S. policymakers to respond by more expansionary macroeconomic policies. It should not be overlooked that stimulating domestic demand sufficiently to offset deflationary forces reaching U.S. shores from abroad is made easier by the benefits enjoyed by the key reserve currency issuer en route: cheap imports and easy terms of finance—given that U.S. dollar reserves normally pay only low rates of interest (on top of offering top-safety as sought by their foreign official holders).

These general insights into the workings of the dollar-centered world monetary and financial order come in handy when investigating critical global developments that led up to the Lehman-triggered financial implosion of 2008, the global policy responses that have followed since, and the prospects for global rebalancing and recovery as they present themselves today. The point I am driving at is that the world monetary and financial order conditioned and induced particular macroeconomic policies in the United States and the rest of the world, policies that led to the buildup of global (and domestic) imbalances and underlying international (and domestic) credit structures. The future outlook for the United States and world economies continues to be contingent upon the dollar's role in the global order, even if a return to conditions and policies prevailing before the crisis seems unlikely.

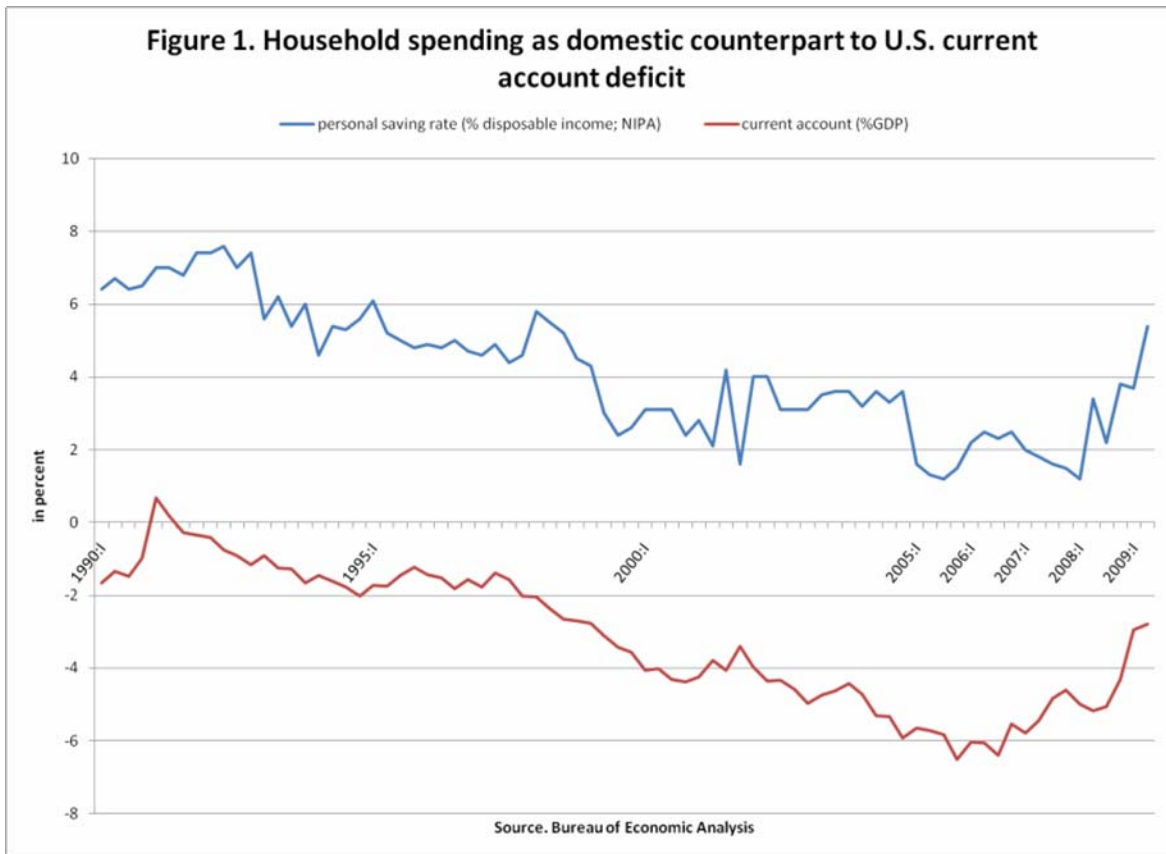
III. BRETTON WOODS II HYPOTHESIS IGNORED BUILDUP OF INTERNAL IMBALANCES

To highlight some critical issues, I will draw on the so-called "Bretton Woods II" (BWII) hypothesis as my framework of analysis. In 2003, Michael Dooley, David Folkerts-Landau, and Peter Garber hypothesized in their influential "Essay on the Revised Bretton Woods System" (or "Bretton Woods II") that global imbalances featuring a quasi-permanent U.S. current account

deficit may be sustainable. In their view, global current account imbalances reflected a symbiosis of interests among deficit (United States) and surplus (developing world) countries. The developing world's interest is to sell its products in the large U.S. market as a way of stimulating employment growth and development. The U.S. economy, on the other hand, is flexible enough to tolerate the resulting quasi-permanent drag on U.S. income growth, given its comparative advantage in creating safe assets that the periphery wishes to accumulate for safety reasons.

Note that the global monetary and financial order stands right at the center of an analysis of global "imbalances" that are actually interpreted as a balanced situation by Dooley, Folkerts-Landau, and Garber (2003). Moreover, the chosen title, "Revised Bretton Woods System," signals that the authors seem to see a lot of continuity in postwar monetary arrangements, despite the fact that the world has moved away from the "Bretton Woods I" system of pegged exchange rates in the 1970s. Dooley, Folkerts-Landau, and Garber (2003) suggest that a new "periphery" (China in particular) has emerged, replacing the former periphery of Western Europe and Japan, in relying on export-led growth strategies by pegging to the U.S. dollar—which has remained the currency at the center of the so-revised global order.

In view of what I said above about the dollar-centered global monetary and financial order, it will come as no surprise that I principally agree with these general points of perspective. However, there is one factor conspicuous for its absence in the BWII hypothesis that turned out to be rather critical to the supposed sustainability of these arrangements. I am referring to those "safe assets," in the production of which the United States has a comparative advantage. It is, of course, true that the official authorities of countries such as China have largely accumulated safe assets, U.S. Treasuries in particular. The point is that the assets that actually sponsored U.S. spending in excess of income growth were assets that have proven to be so lethally "toxic" as to cause a global crisis.



The BWII hypothesis ignores that the domestic counterpart to the U.S.'s external deficit was based not on (safe) public debts, but on (toxic) private debts, mortgage debt in particular. Skepticism regarding soaring household indebtedness and the implications for the solvency of lenders ended the party when underlying collateral values stopped rising in 2006. In essence, as foreign official authorities came to hold a rising share of the outstanding stock of U.S. Treasuries, U.S. consumer spending was fired by households taking on ever more debt relative to income. The rise in household indebtedness (leverage) saw the U.S. personal saving rate decline from about 10 percent in the 1980s to little more than zero by 2007.[2] While falling interest rates helped keep the private debt burden in check to some extent, trends like these can clearly not continue forever. Figure 1 shows that previous trends of a declining saving rate and rising external deficit reversed in 2006–07. To be sure, U.S. households will not pay down debt forever. They will start borrowing again at some point. The point is that we are unlikely to see a

[2] The Levy Institute's periodic "Strategic Analysis" publications warned of the unsustainability of these trends. See for instance, Godley et al. (2007).

return to and continuation of previous patterns of behavior featuring a continuous decline in the saving rate.[3]

IV. THE U.S. CONSUMER AS "GLOBAL BORROWER AND SPENDER OF LAST RESORT"

Let me highlight then how the world monetary and financial order nurtured the U.S. consumer in its role as "borrower and spender of last resort," the true engine of growth behind the BWII system. In the early 1990s, Japan was the first calamity in the world economy that created forces for overspending in the United States. Stuck in protracted domestic demand stagnation, Japan has become wholly reliant on exports for its meager GDP growth. Germany came next, following the Bundesbank-provoked recession in response to the country's unification. Ever since 1993, Germany has also relied only on its export engine. Germany's influence in the global economy became further magnified when its economic policy model was exported to Europe through the Maastricht Treaty on Economic and Monetary Union—effectively committing Europe to a mercantilistic model of growth. The detrimental effects of the spreading of the "German disease" have become most visible in "Euroland," the club of countries that have adopted the euro as their common currency. Domestic demand had stagnated for much of the 1990s and "between 2001 and 2005, the eurozone was the sick giant of the world economy" (Wolf 2007; see also Bibow [2009b]). Note that these countries are all industrialized competitors of the United States. According to the BWII hypothesis, these countries should have long matured and no longer be part of any export-led growth "periphery."

A new periphery really only came to emerge in the aftermath of the 1997–98 Asian crises, events that seem to have convinced increasing numbers of developing countries to seek safety in pursuing current account surplus rather than deficit positions. China, which had already

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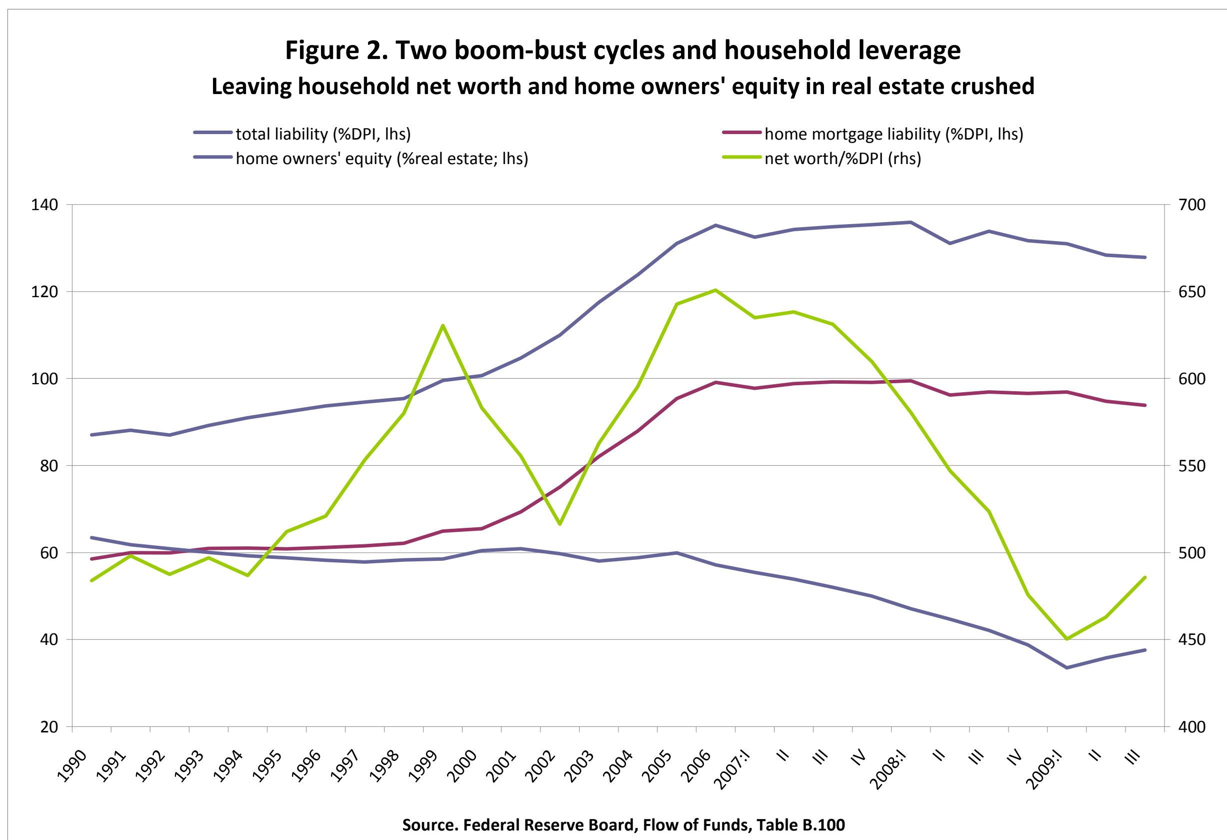
[3] Dooley, Folkerts-Landau, and Garber (2008) confirm their position on a symbiosis of interests that would continue to permit large U.S. current account deficits financed at low real risk-free rates, predicting only "a gradual reduction over the course of at least five more years as managed currencies gradually appreciate." Dooley, Folkerts-Landau, and Garber (2009) assert that "the incentives that drive the Bretton Woods II system will be reinforced by the crisis and, looking forward, participation in the system will expand and the life of the system will be extended." In their view, "emerging markets will be even more convinced that reserve accumulation and export-led growth are the safest development strategy in an uncertain world." They list Bibow (2009a) on "The Emerging Contours of BWIII" among their references, but expect that beyond a brief interim period during which fiscal stimulus may have to carry the torch, "U.S. households will partly return to a relatively low savings, debt building, equilibrium," merging back onto previous BWII paths.

pegged to the dollar in 1994 and maintained a competitive exchange rate ever since, represents one prominent example in this group, but China's current account surplus has really only soared since 2003 (Bibow 2007). Especially in the years 2006–08, oil producers turned into another important group of current account surplus countries and dollar investors.

Recall that in a world that becomes ever keener to export and accumulate dollars, systemic deflationary forces mount and hit the domestic economy of the key reserve currency issuer by putting downward pressure on wages and prices in general. In fact, without any offsetting forces forthcoming from U.S. macroeconomic policies, U.S. and world economies would have faced the prospect of deflation. In the event, U.S. macro policies have responded flexibly to the above external developments since global imbalances started to emerge in the early 1990s, with monetary policy as a first line of defense and recourse to active fiscal policy restricted to outright recessions. The Federal Reserve's mandate features maintaining price stability and high employment. Monetary policy encourages private spending by lowering interest rates, easing credit, and boosting asset prices. The Fed would have failed on both counts if it had not eased its policy stance sufficiently. In actual fact, the Fed battled the jobless recovery following the 2001 recession with fervor, keeping rates at low levels for a sustained period of time. Rising household indebtedness seemed fine as long as net worth kept on rising, too. Figure 2 shows that after recovering from the tech bust, household net worth was, once again, severely crushed and fell back to the early 1990s level relative to disposable income, albeit this time at higher levels of household indebtedness, driven by home mortgages and fallen home equity shares.



It is easy today to blame the Fed for causing bubbles. It is harder to see how the Fed could have otherwise fulfilled its mandate when global conditions were such that deflationary forces arriving from abroad required an offset from U.S. domestic demand that was not provided by public spending. The emergence of global imbalances, featuring a rising U.S. current account deficit, was thus inherently entwined with the emergence of domestic imbalances—debt-financed consumer spending and rising household indebtedness in particular. In 2006, projections by the IMF and OECD still showed a continued rise of the U.S. current account as a share of GDP. I argued above that the internal trends required to meet such projections were unsustainable—the aspect ignored in the BWII hypothesis. BWII was doomed long before Lehman hit the wall; the bank's failure merely delivered the regime's death blow.[4]

[4] These issues are investigated in more depth and detail in Bibow (2009c).

V. THE EMERGENCE OF BRETTON WOODS III?

Since the Lehman crisis, imbalances have shrunk sharply in the context of the freefall in global trade and industrial production and the policy responses that the Lehman crisis has triggered across the globe. While U.S. fiscal stimulus has been decidedly stronger than in Europe, China has emerged as lead engine of recovery in Asia. Massive Chinese fiscal stimulus and credit expansion have propelled domestic demand (and imports) and offset a good part of the decline in exports (and net exports growth contribution). Moreover, rock-bottom U.S. interest rates have greatly enlarged the leeway for easier financial conditions in many emerging markets. So perhaps the emerging market consumer may be expected to step up to the bar and carry the torch for global growth from here on?

Beyond the short term, I doubt that the global economy would operate smoothly along these lines for long (see Kregel [2004]). In fact, we may already be sowing the seeds for new financial accidents to happen in the developing world—which would be a return to 1990s patterns. I suspect that key emerging market governments, keenly aware of this risk, may therefore prefer to continue to resort to defensive macroeconomic policies. The trouble is, however, that for quite some time the U.S. consumer will not be in any shape to resume his/her previous behavior. So what could be the new engine of U.S. and global growth?

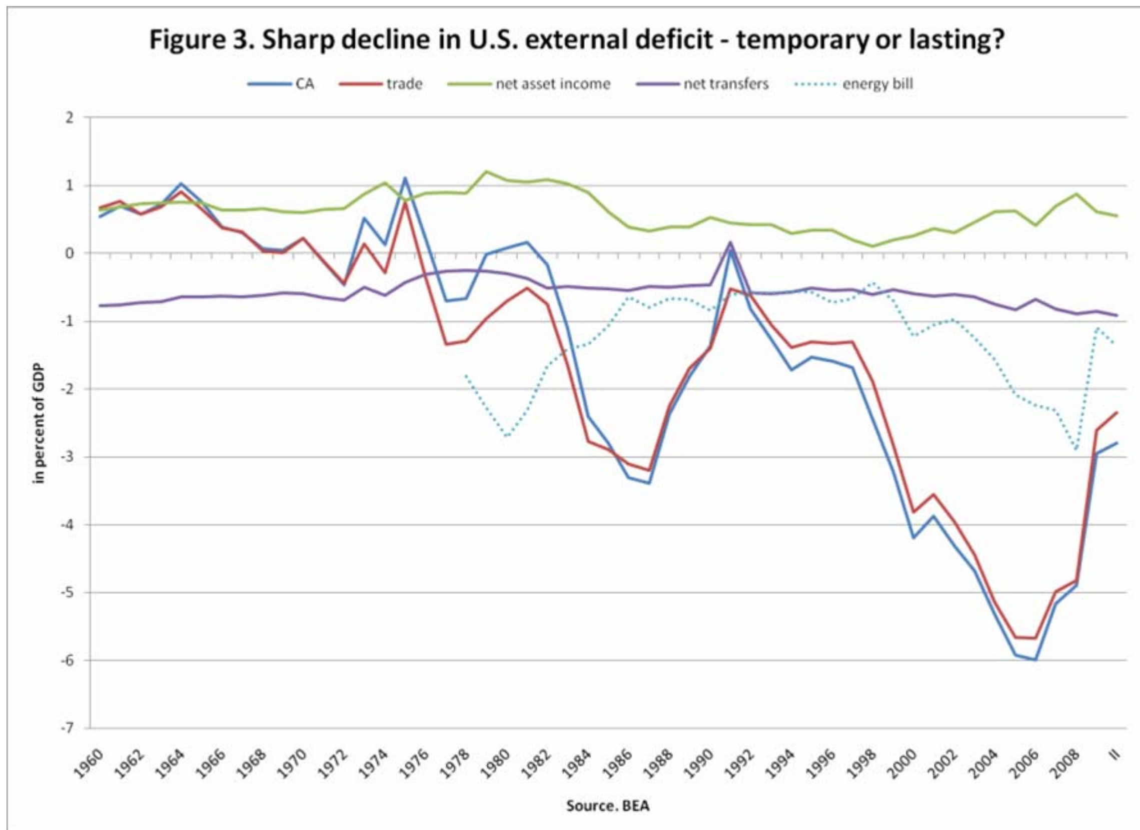


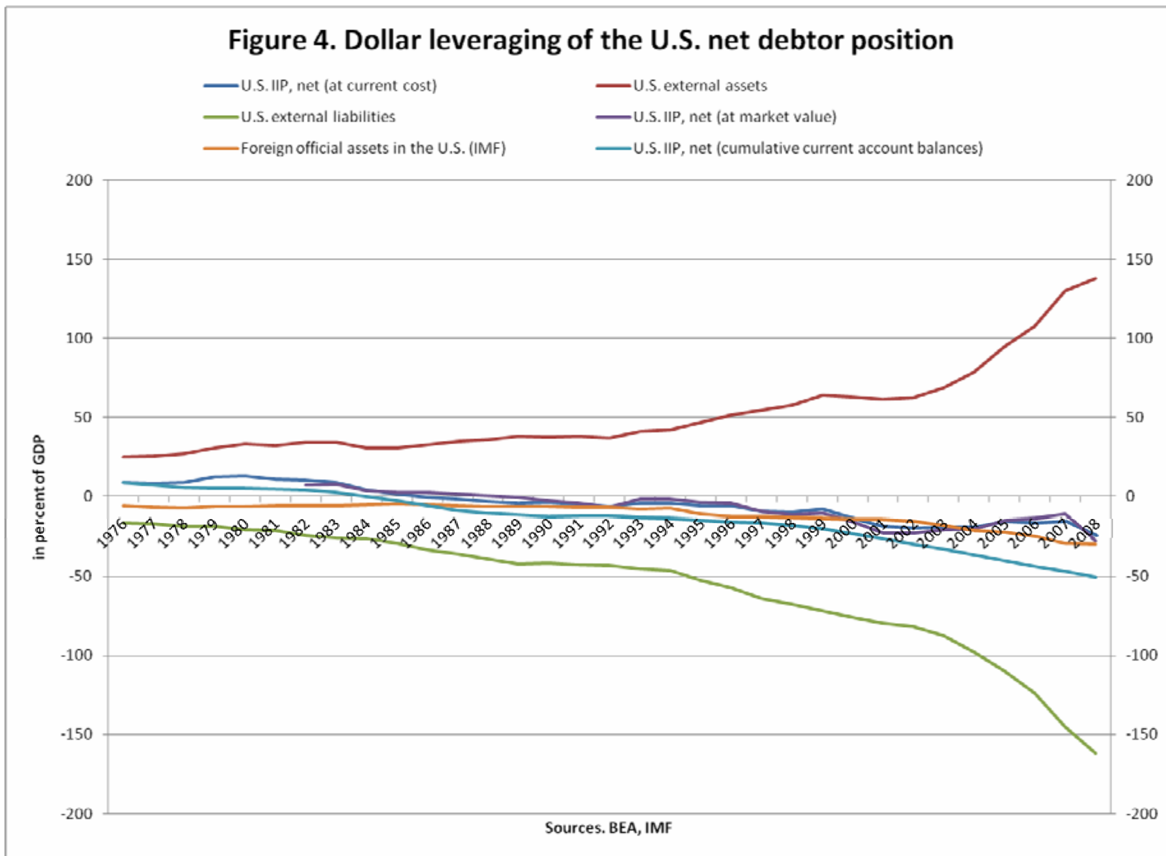
Figure 3. Sharp decline in U.S. external deficit - temporary or lasting?

Interestingly, while BWII is certainly dead, a new "Bretton Woods III" (BWIII) regime might be in the process of emerging in its stead. Under BWIII, U.S. public debt replaces private debt. The change of guard from monetary policy to fiscal policy has come about in the first place by the sheer severity of the crisis. With monetary policy short on ammunition and important parts of the financial system dysfunctional, the only way to support domestic demand is to cut taxes in support of private incomes and spending or to boost public spending itself. As the private sector retrenches brutally, the public sector has to carry the torch or else witness the economy sink into the abyss. In the winter of 2008–09 the world economy and world trade experienced a freefall comparable to the Great Depression of the 1930s. In contrast to that earlier episode, however, governments around the world initiated fiscal stimulus programs, although with some regional variation in magnitude. Figure 3 shows that the U.S. current account deficit has more than halved from its peak of 6 percent of GDP in 2006 to below 3 percent in the first half of 2009. The question is whether the current global rebalancing and unwinding of imbalances is really going to continue, vindicating White House economics director Larry

Summers' (2009) call for the United States to switch its consumption-based growth model for an export-oriented one.

I argued above that U.S. macroeconomic policies are conditioned by policies pursued in the rest of the world. If the United States were to merge in the export-led growth lane, already overcrowded by the rest of the world, this would set the world on collision course, a sure recipe for disaster. It would also mean a refusal by the United States to play its role as key reserve currency issuer. If the rest of the world resumes its previous policy patterns of aspiring to current account surplus positions and dollar reserve accumulations, the real choice facing the United States as key reserve currency issuer is to take recourse to fiscal policy and public debt rather than trying to rekindle the emergence of private sector imbalances. While we currently view fiscal policy as providing no more than a temporary emergency boost to restart private spending, BWIII would actually imply a more lasting role for fiscal policy in sustaining domestic demand.

To be sure, I do not mean anything like the current deficits, in double digits, as a share of GDP. These stunning numbers reflect, first and foremost, the magnitude of ongoing private sector retrenchment. Public deficits will shrink as the private sector rebalances over the next few years. Even beyond this short-term rebalancing, more permanent budget deficits may be needed if the rest of the world were to resume previous policies. National income accounting implies that if the private sector's financial balance were balanced again, any U.S. current account deficit would require a corresponding public sector deficit. While a return to rising current account deficits of 6 percent of GDP or so would likely quell renewed troubles not too far down the road, deficits of, say, 3 percent may be perfectly manageable. Assuming 6 percent nominal GDP growth, the U.S. net international investment position would converge to (negative) 50 percent of GDP in the long run.



With rising external indebtedness, a crucial issue concerns U.S. external financing costs, and it is in this regard that the comparative advantage of the United States in producing low-yielding safe assets comes in handy. In contrast to BWII, the safe assets acquired by foreign official authorities would also be the very assets that actually sponsor U.S. spending in excess of income: public debt (or government guaranteed securities) rather than private debt. Under BWII, Fed monetary policy played the lead role in keeping interest rates low, credit easy, and asset prices high and rising to induce sufficient private spending fired by private debts. Under BWIII, Fed policy would still be important in keeping interest rates and public debt financing costs, both internally and externally, low. Internally, accommodative Fed policies are needed to keep the interest burden on the public debt at bay and to maintain the scope for running primary deficits. From the postwar period until the “Volcker shock,” the interest rate paid on the public debt fell well short of the nominal GDP growth rate (Darby 1984), allowing favorable debt dynamics (Domar 1944).

Externally the situation is quite similar in that high demands for low-yielding Treasuries in the rest of the world help the United States in running a persistent trade deficit. Another factor is important in explaining the fact that the United States has actually maintained a positive investment income balance on their current account (see figure 3) despite having a sizeable negative net international investment position (as shown in figure 4), namely "dollar leveraging."

The point is that the United States enjoys a "rate of return advantage" on its gross foreign assets over its gross foreign liabilities, so that leveraging its negative net foreign asset position can actually produce positive investment income—securing the scope for persistent trade deficits. Part of the rate of return advantage arises from "composition effects," as the composition of U.S. foreign assets is overweight in higher-yielding and riskier assets compared to its predominantly lower-yielding foreign liabilities—those safe assets featuring in BWII. It is, however, noteworthy that only part of the excess return takes the form of an income yield advantage. Valuation (capital) gains, too, are very important, partly arising from exchange rate changes as dollar depreciation delivers positive valuation gains in the U.S. case (much in contrast to emerging market countries committing the original sin of borrowing in a foreign currency). Figure 4 reveals that valuation gains have kept the deterioration of the U.S. net debtor position well short of what cumulative current account deficits would have otherwise implied.[5] Looking forward, the Federal Reserve and a rebooted Wall Street would have to play an important assisting role in sustaining low U.S. financing costs, but under BWIII fiscal policy would take on the lead role in sustaining domestic demand—a change of guard in macroeconomic policy.

One must, of course, not overlook the irony in all this: if global growth should really depend on continuous trade deficits on the part of the global reserve currency issuer, dollar leveraging would seem to critically assist in sustaining that arrangement. In other words, unfettered global finance may have both increased the demand for defensive policies in the rest of the world as well as the extraction of rent available from meeting that demand (Bibow 2009e).

VI. A FUTURE BRETTON WOODS IV?

Importantly, as under BWII, the need and scope for BWIII "imbalances" (i.e., the size of the "equilibrium" U.S. current account deficit) largely depends on macro policies in the rest of the

[5] For a more in-depth analysis of the sustainability issue, see Bibow (2009e) and the literature referred to there.

world. If, finally, Japan and Germany were really to mature from the mercantilistic periphery and generate domestic demand-led growth, this would take important pressure off the U.S.'s shoulders. The same effect would occur if developing countries decided that globalization has become safer—perhaps due to reforms to global finance and the IMF with greater provision of "collective insurance." Finally, if China learned from its own ongoing rebalancing in the context of massive fiscal stimulus measures and credit expansion that a greater reliance on domestic, rather than external, demand is in its own national interest, this too would reduce the need and scope for BWIII accordingly.

One may therefore venture some speculations about longer term prospects for the world monetary and financial order. At some point in the future, all major regions and players might mature and pursue domestic demand-led growth while exchange rates are adjusted so as to keep global trade in balance. The future order is conceivable without any key reserve currency playing the crucial role currently occupied by the dollar if international liquidity were organized as a concerted effort by the global community.

The dollar is not likely to retain its current special status forever.[6] BWIII may, however, offer a more stable and sustainable system for the transition towards a more balanced "Bretton Woods IV" system of equal partners. As alternative arrangements along these lines would correspond to Keynes's original vision for the postwar order developed in the early 1940s, we could also call them "Bretton Woods 0" for that reason—the global order that never came to be as the actual "Bretton Woods I" was dollar-centered from the beginning.

Even without any official "new Bretton Woods" agreement, the alternative arrangements just sketched may still come about by market evolution and policy adaptation as China, India, and perhaps even Europe mature to a more equal global status, but this prospect still seems a matter of decades. In the interim period, BWIII might provide a more sustainable regime than BWII could have ever become. If other countries do not like the prospect of continuous U.S. budget deficits, they can let their exchange rates appreciate, wean themselves off U.S.-sponsored export growth, and adopt domestic demand-led growth on their own. This is the real choice countries such as China are facing. Figure 4 also shows the role of foreign official assets in the United States as a prominent counterpart of U.S. current account deficits and private capital

[6] For recent contributions on the issue of reforming the international monetary and financial system, see Galbraith (2009) and Kregel (2009), for instance.

outflows. A dollar collapse, as feared by critics of BWII, seems distinctly unlikely for lack of any real alternative. In principle, this is no different under BWIII. Absent any official "new Bretton Woods" agreement, the dollar will be bereaved of its unchallenged position at the hub of the global monetary and financial order only gradually as other powers catch up and mature.

VII. DOMESTIC POLICY OPTIONS

The United States cannot force other countries' policy choices, but in fulfilling its role as reserve currency issuer they should design their own macroeconomic policies in ways that best serve the national interest. The analysis here suggests that in order to avoid igniting yet another private debt-driven boom-bust cycle, fiscal policy, rather than monetary policy, should be used to sustain U.S. domestic demand growth. Yet, simply applying income tax cuts to boost disposable incomes and consumer spending would just turn (would-be) private debt-financed HD television purchases (under precrisis conditions) into public debt-financed gifts of such goods, with not much else required to change in the domestic and global economies.

A far better way of applying fiscal policy would be to boost public spending with a focus on infrastructure investment instead. Infrastructure investment offers the prospect of boosting U.S. income growth in a more sustainable fashion while helping the United States to stay competitive relative to rising foreign nations (see Heintz, Pollin, and Garret-Peltier [2009] and Pollin and Garret-Peltier [2009], for instance). Surely there is no economic reason why yet another debt-financed HD television should be more beneficial to long-term U.S. growth than a debt-financed upgrade of U.S. infrastructure. Yet a compositional shift in U.S. spending would imply structural changes in the U.S. and global economies as U.S. consumer spending would permanently stay below its previous trajectory, which would hurt the corresponding industries at home and abroad. At the same time, depending on the home content of infrastructure investment, a compositional shift in demand might well help to contain the U.S. current account deficit and keep it at a sustainable level.

In particular, note that apart from boosting U.S. growth, infrastructure initiatives to raise U.S. energy security would at the same time help to contain a resurging U.S. energy (import) bill, a factor that inflated the U.S. current account deficit in the last boom (see figure 4).

Flexibility, open-mindedness, and creativity are needed in filling the proper role for infrastructure investment in BWIII.

VIII. CONCLUDING REMARKS

The global crisis of 2007–09 was ultimately rooted in the world monetary and financial order and the macroeconomic policies and global imbalances induced by that global order. BWII, featuring private debt-financed consumer spending as the counterpart to the U.S.'s external deficit, is dead and cannot easily be revived, but a BWIII regime may come to take its place, featuring continued U.S. current account deficits, this time driven by public spending and public debt. Unlike under BWII, under BWIII the safe assets accumulated by the periphery's official authorities would also be the very assets actually sponsoring U.S. spending in excess of income. While U.S. fiscal policy takes on the lead role in sustaining domestic demand under BWIII, Federal Reserve policy and—somewhat ironically—a rebooted Wall Street would need to play assisting roles in keeping U.S. financing costs low to secure the sustainability of the arrangement. Policy choices in the rest of the world would determine the need and scope for the United States to operate along BWIII arrangements for as long as the U.S. dollar remains the world's key reserve currency.

Alternative arrangements under which the U.S. dollar would lose its special status as other key countries mature are conceivable, but—absent any such official agreement—may still take decades to come about by evolution. In the interim, BWIII might actually offer more sustainability and greater benefit if the United States were to adapt macroeconomic policies accordingly and focus on upgrading domestic infrastructure.

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