Financial Crises, Global Capital Flows and the International Financial Architecture

By Sam Vaknin, Ph.D.

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The recent upheavals in the world financial markets were quelled by the immediate intervention of both international financial institutions such as the IMF and of domestic ones in the developed countries, such as the Federal Reserve in the USA. The danger seems to have passed, though recent tremors in South Korea, Brazil and Taiwan do not augur well. We may face yet another crisis of the same or a larger magnitude momentarily.

What are the lessons that we can derive from the last crisis to avoid the next?

The first lesson, it would seem, is that short term and long term capital flows are two disparate phenomena with very little in common. The former is speculative and technical in nature and has very little to do with fundamental realities. The latter is investment oriented and committed to the increasing of the welfare and wealth of its new domicile. It is, therefore, wrong to talk about "global capital flows". There are investments (including even long term portfolio investments and venture capital) – and there is speculative, "hot" money. While "hot money" is very useful as a lubricant on the wheels of liquid capital markets in rich countries – it can be destructive in less liquid, immature economies or in economies in transition.

The two phenomena should be accorded a different treatment. While long term capital flows should be completely liberalized, encouraged and welcomed – the short term, "hot money" type should be controlled and even discouraged. The introduction of fiscally-oriented capital controls (as Chile has implemented) is one possibility. The less attractive Malaysian model springs to mind. It is less attractive because it penalizes both the short term and the long term financial players. But it is clear that an important and integral part of the new International Financial Architecture MUST be the control of speculative money in pursuit of ever higher yields. There is nothing inherently wrong with high yields – but the capital markets provide yields connected to economic depression and to price collapses through the mechanism of short selling and through the usage of certain derivatives. This aspect of things must be neutered or at least countered.

The second lesson is the important role that central banks and other financial authorities play in the precipitation of financial crises – or in their prolongation. Financial bubbles and asset price inflation are the result of euphoric and irrational exuberance – said the

Chairman of the Federal Reserve Bank of the United States, the legendary Mr. Greenspun and who can dispute this? But the question that was delicately side-stepped was: WHO is responsible for financial bubbles? Expansive monetary policies, well timed signals in the interest rates markets, liquidity injections, currency interventions, international salvage operations – are all co-ordinated by central banks and by other central or international institutions. Official INACTION is as conducive to the inflation of financial bubbles as is official ACTION. By refusing to restructure the banking system, to introduce appropriate bankruptcy procedures, corporate transparency and good corporate governance, by engaging in protectionism and isolationism, by avoiding the implementation of anti competition legislation – many countries have fostered the vacuum within which financial crises breed.

The third lesson is that international financial institutions can be of some help – when not driven by political or geopolitical considerations and when not married to a dogma. Unfortunately, these are the rare cases. Most IFIs – notably the IMF and, to a lesser extent, the World Bank – are both politicized and doctrinaire. It is only lately and following the recent mega-crisis in Asia, that IFIs began to "reinvent" themselves, their doctrines and their recipes. This added conceptual and theoretical flexibility led to better results. It is always better to tailor a solution to the needs of the client. Perhaps this should be the biggest evolutionary step:

That IFIs will cease to regard the countries and governments within their remit as inefficient and corrupt beggars, in constant need of financial infusions. Rather they should regard these countries as CLIENTS, customers in need of service. After all, this, exactly, is the essence of the free market – and it is from IFIs that such countries should learn the ways of the free market.

In broad outline, there are two types of emerging solutions. One type is market oriented – and the other, interventionist. The first type calls for free markets, specially designed financial instruments (see the example of the Brady bonds) and a global "laissez faire" environment to solve the issue of financial crises. The second approach regards the free markets as the SOURCE of the problem, rather than its solution. It calls for domestic and where necessary international intervention and assistance in resolving financial crises.

Both approaches have their merits and both should be applied in varying combinations on a case by case basis.

Indeed, this is the greatest lesson of all:

There are NO magic bullets, final solutions, right ways and only recipes. This is a a trial and error process and in war one should not limit one's arsenal. Let us employ all the weapons at our disposal to achieve the best results for everyone involved.

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Lawsuit Loans

By Wensley McKenney

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Lawsuit Loans which are also known as pre settlement cash advances allow a financially strapped plaintiff to access a portion of their future legal settlement to pay today's necessary living expenses. Personal Injury and worker compensation lawsuits can take years to resolve and large insurance companies have the financial strength to legally delay the process which can financial ruin an injured claimant who is looking for a fair settlement offer.

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The fees charge by lawsuit loan companies can vary dramatically but it is usually best to stick with the larger companies, like Global Financial (http://www.glofin.com) because they work on larger volumes and lower pricing. Usually a funding company will charge either a monthly fee or a flat fee depending on the risk associate with the claim.

It is my personal opinion that a claimant should ask themselves one question before applying for a cash advance against their pending claim. Will the advance that I receive pay immediate and necessary living expense? If the answer is yes then you should accept a cash advance and continue with your legal claim. If the answer is no then it might be wise to hold off and wait before applying for a lawsuit loan or cash advance against your pending claim. In addition, a lawsuit loan may be a very important tool when the defendant's insurance carrier decides to make a low ball offer for settlement in the claim. You can then use a lawsuit loan as a financial tool to say no to the low ball offer and have the financial strength to wait for a higher and fairer settlement.

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Wensley McKenney is a graduate of Tulane University and has 15 years of experience in the financial and legal fields.

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