UN Says New Currency Is Needed to Fix Broken 'Confidence Game'

By Jonathan Tirone

Sept. 7 (Bloomberg) -- The dollar's role in international trade should be reduced by establishing a new currency to protect emerging markets from the "confidence game" of financial speculation, the United Nations said.

UN countries should agree on the creation of a global reserve bank to issue the currency and to monitor the national exchange rates of its members, the Geneva-based UN Conference on Trade and Development said today in a report.

China, India, Brazil and Russia this year called for a replacement to the dollar as the main reserve currency after the financial crisis sparked by the collapse of the U.S. mortgage market led to the worst global recession since World War II. China, the world's largest holder of dollar reserves, said a supranational currency such as the International Monetary Fund's special drawing rights, or SDRs, may add stability.

"There's a much better chance of achieving a stable pattern of exchange rates in a multilaterally-agreed framework for exchange-rate management," Heiner Flassbeck, co-author of the report and a UNCTAD director, said in an interview from Geneva. "An initiative equivalent to Bretton Woods or the European Monetary System is needed."

The 1944 Bretton Woods agreement created the modern global economic system and institutions including the IMF and World Bank.

Enhanced SDRs

While it would be desirable to strengthen SDRs, a unit of account based on a basket of currencies, it wouldn't be enough to aid emerging markets most in need of liquidity, said Flassbeck, a former German deputy finance minister who worked in 1997-1998 with then U.S. Deputy Treasury Secretary Lawrence Summers to contain the Asian financial crisis.

Emerging-market countries are underrepresented at the IMF, hindering the effectiveness of enhanced SDR allocations, the UN said. An organization should be created to manage real exchange rates between countries measured by purchasing power and adjusted to inflation differentials and development levels, it said.

"The most important lesson of the global crisis is that financial markets don't get prices right," Flassbeck said. "Governments are being tempted by the resulting confidence game catering to financial-market participants who have shown they're inept at assessing risk."

The 45-year-old UN group, run by former World Trade Organization chief Supachai Panitchpakdi, "promotes integration of developing countries in the world economy," according to its Web site. Emerging-market nations should consider restricting capital mobility until a new system is in place, the group said.

The world body began issuing warnings in 2006 about financial imbalances leading to a global recession.

The UN Trade and Development report is being held for release via print media until 6 p.m. London time.

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