



*PRIME RESEARCH PUBLICATION NO. 90*

# TRUMP'S TARIFFS AND THE GHOST OF KEYNES: 81 YEARS LATER, VINDICATION OR REPETITION?

**DR MOHAMMAD AHMED ZUBAIR**

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Prime Institute

House #01, Street # 58, F-7/4

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Tel: 00 92(51) 8 31 43 38

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# Trump's Tariffs and the Ghost of Keynes: 81 Years Later, Vindication or Repetition?

By

**Dr Mohammad Ahmed Zubair**

## Abstract

This paper revisits the Trump administration's imposition of tariffs—branded as "Liberation Day" tariffs—as a watershed moment in the long arc of American trade exceptionalism and a vivid manifestation of unresolved global economic contradictions first identified by John Maynard Keynes over eight decades ago. Far from being a radical departure, Trump's tariff strategy is situated within a historical continuum in which the United States has repeatedly recalibrated global economic rules in response to domestic vulnerabilities and shifting geopolitical conditions. The paper draws a parallel between past crises—such as the Roosevelt administration's 1933 gold suspension and Nixon's 1971 abandonment of the gold-dollar standard—and the contemporary retreat from multilateral trade norms. Using this long-wave historical lens, the paper argues that the breakdown of symmetrical adjustment mechanisms, especially in the U.S.–China trade relationship, has exposed the fragility of the current international economic order. China's persistent surpluses and the United States' structural deficits are not merely technical imbalances; they are the outcome of deeper institutional and strategic divergences between financial capitalism and state-led industrialism.

The paper offers a critical reassessment of the Bretton Woods framework, emphasizing Keynes' original insight that global economic stability requires shared responsibility for adjustment by both surplus and deficit countries. It critiques the failure of key multilateral institutions—particularly the IMF and WTO—to enforce this principle, arguing that the erosion of their authority has allowed imbalances to persist and become structurally entrenched resulting in geopolitical tensions to escalate. Through an examination of recent IMF External Sector Reports and bilateral surveillance assessments, the study reveals both diagnostic clarity and procedural impotence. As a concrete reform proposal, the paper recommends the creation of a "Policy Coordination Action Matrix," rooted in IMF assessments and integrated into the G20 process, to enhance accountability and ensure symmetry in global adjustment efforts. The paper further advocates for a new approach to global governance that restores the centrality of the state, prioritizes democratic legitimacy, and recalibrates economic multilateralism to accommodate in a multipolar world. Ultimately, the paper contends that the Trump-era tariffs, while disruptive, have reignited necessary debates about fairness, adjustment, and institutional reform—demonstrating that Keynes's vision remains both relevant and unrealized. Eighty-one years later, the ghost of Keynes haunts a global system still grappling with the same fundamental asymmetries.

**Key Words:** U.S. trade policy, Liberation Day tariffs, global economic imbalances, Keynesian policy legacy, Bretton Woods reform, strategic industrial policy, trade multilateralism, IMF surveillance, WTO reform, G20 economic coordination, international trade governance, global macroeconomic adjustment.

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## About the Author:

**Dr. Zubair is a former Chief Economist at the Planning Commission, Government of Pakistan. He also served as Regional Lead Economist at the Islamic Development Bank in Jeddah. He is currently a Research Fellow at the PRIME Institute in Islamabad.**

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## Introduction

1. President Trump announced 'Liberation Day' expansive tariffs on 2nd April, followed subsequently by additional retaliatory tariffs, which has sent shock waves across the businesses and stock markets around the world. On 10th April, Trump administration has announced that, except for China, a temporary suspension of further tariff measures and a stated willingness to pursue a new bilateral trade arrangements with a number of various trading blocs and individual nations.
2. It is evident that initiation of reciprocal tariffs by Trump administration was both unprecedented in scope and disruptive in its implications. For too long, post WW-II multilateral system failed to address a fundamental challenge: the lack of resolve by the "creditor" countries to engage with the "debtor" countries to address persistent and unsustainable or untenable build-up of trade imbalances. However, it must also be acknowledged that the post WW-II global trade and financial architecture, as institutionalized by both WTO and IMF, will have to be substantially redesigned.
3. This research paper seeks to uncover historical origin of various episodic international payments crises and, in the contemporary context, to explain the core reasons of why this failure of global trade policy coordination persisted for so long. By using 'historical long wave' framework, the latest Trumpian tariff move appears as a series of episodes where the US has never hesitated to unilaterally upending or reneging on international economic arrangements and commitments. Post WW-I, the US along with its second-tier of *allies or the coalition of the willing* has always acted to design an international economic and monetary system that best suited its position as a global economic hegemon. Seen in this way, Trumpian retaliatory tariffs and upending of current global trading system should not appear shocking or surprising. Except that, for the first time, US is now locked in a symmetrical economic warfare.
4. Yes, Trump tariffs is man made crisis and is in violation of WTO rules. Yet, the origins of present-day monumental crises lie in the basic faulty design of global trade and payments system. Also, global crises of such magnitude have occurred in the past and were forewarned by Lord John Maynard Keynes during the Bretton Woods (BW) conference in 1944. Keynes argued that unless there is an international mechanism to address persistent global imbalances (i.e. perennial trade deficits in one group of countries and trade surpluses in another group of countries), maintenance of global free trade regime will not be politically tenable or sustainable. Moreover, to correct global trade imbalances, the burden of adjustment needs to fall on trade surpluses group of countries.
5. Keynes argument was that it is not politically feasible for trade deficit group of countries to bear the entire adjustment costs as it will lead to intolerable levels of national unemployment. Moreover, both the post-BW institutions have also failed to bring about a multilateral and sustainable reform of the system - the WTO, for variety of reasons, has singularly failed to effectively address resolving global trade imbalances. One reason of this failure is absence of clarity in terms of institutional mandate and enforcement authority between IMF and WTO. What Trumpian tariffs move has demonstrated is basically a vindication of Keynes concerns after 81 years.

## Keynes during Inter-War Period

6. The inter-war period (November, 1918-September, 1939) was interspersed with severe economic and financial turmoil in cross-Atlantic countries like multiple episodes of recession, massive unemployment, banks' failures, suspension of currency convertibility, 'beggar-thy-neighbour' policy of competitive currency devaluation, sovereign debt defaults, reconstruction costs in war-torn countries, and unsustainable reparations burden on Germany. During this period, Keynes was active in academic publications, policy advocacy at the highest levels in Europe and USA, and public and media engagements. Keynes viewed all this as "*the political problem of mankind: how to combine three things: economic efficiency, social justice and individual liberty*" (Essays in Persuasion, 1931).

7. Keynes essay, *National Self-Sufficiency* is prescient today as it was back in June 1933. The context of the essay was deepening of great depression, which was failure of capitalism and rising authoritarian regimes, resulting from fascists and communists gaining political grounds. Keynes did not support unfettered free trade because, he thought, it had the potential to lead to persistent trade imbalances which, in turn, exacerbate domestic unemployment and economic growth, as well as result in domestic political backlash and, at worse, create acrimonious conflicts among nations.

8. Essentially, Keynes was deeply concerned over countries using international trade as desperate attempt to promote domestic employment and shift the adjustment burden (principally in the form of austerity measures) to trade deficit countries.<sup>1</sup> In this vein, Keynes critiqued ideas of global financial capitalism, argued that countries reduce and moderate dependence on financial globalization, and made it clear that he was not advocating isolationism but favoured a more balanced and thoughtful approach to national economic policy.

9. Immediately after his inauguration in March 1933, President Franklin Roosevelt announced *the New Deal*, which was expansive reform program for banking sector, emergency relief, agriculture, social security, aid assistance to tenant farmers and migrant workers, and various public works programs. At the request of *The New York Times*, Keynes wrote a detailed and an open letter addressed to President Roosevelt in December 1933.

10. In the letter addressed to Roosevelt, Keynes displayed his genius and proffered policy advice on how to prioritize and sequence the implementation pace of 'recovery from the slump' and 'long overdue business and social reforms', essentially supported deficit spending by borrowing funds and not taxing current incomes, warned against pursuing restrictive monetary policy, and alerted to be wary of various vested groups.

11. Keynes also stated in the letter that "*But exchange depreciation should follow the success of your domestic price-raising policy as its natural consequence, and should not be allowed to disturb the whole world by preceding its justification at an entirely arbitrary pace....The currency and exchange policy of a country should be entirely subservient to the aim of raising output and employment to the right level. But the recent gyrations of the dollar have looked to me more like a gold standard on the booze than the ideal managed currency of my dreams*". In other words, Keynes displayed exceptional foresight in warning Roosevelt against the devastating consequences of *engineering* recovery from deep depression in the US through *artificial* 'beggar-thy-neighbour' policy of competitive currency devaluation.

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<sup>1</sup> Davidson, Paul (2011): The Keynes Solution for Preventing Global Imbalances; paper presented at conference "From Crisis to Growth? The Challenges of Imbalances, Debt and Limited Resources; hosted by Research Network on Macroeconomics and Macroeconomic Policies; Berlin, Germany (see page 4).

12. In the midst of cross-Atlantic political chaos, economic turmoil and policy incoherence, Keynes published his magnum opus *The General Theory of Employment, Interest and Money* in 1936, which laid the foundation of theoretical macroeconomic framework and, in the context of collapse of aggregate demand, provided a rationale for increased government spending as a policy instrument for restoring growth and employment. However, it is perplexing that *The General Theory* account of the need to reform the international trade and monetary system has historically remained outside contemporary policy discussions.

13. In *The General Theory*, the central monetary idea is that part of income from growth in output also leads to accumulation of financial assets. The most liquid financial asset is money, which in times of heightened economic uncertainty, leads to increased propensity to hoard. In the context of international monetary system, Keynes objected to gold-standard monetary system on the grounds that, in the context of persistent payments imbalances, the national governments, with persistent balance of payments surpluses, focussed on increased hoarding of precious metal which then, in turn, had a deflationary impact on the global economy.<sup>2</sup>

14. Instead, Keynes argued that an efficient international monetary system would discourage countries to hoard gold, on the back of export-led growth, in a way to spread the burden of adjustment *equitably* between surplus and deficit countries. Keynes proposed a self-corrective or a symmetrical adjustment mechanism through the establishment of an *international clearing union* in which surplus and deficit countries would be both required to rectify imbalances and prevent hoarding of gold.<sup>3</sup>

## Keynes in Bretton Woods (BW)

15. The post WW-II design of international economic and monetary system was stretched over 22 days of intense negotiations in Mount Washington Hotel in Bretton Woods (BW), New Hampshire (USA) in July of 1944. This meeting, which was officially known as the United Nations Monetary and Financial Conference, was attended by 730 delegates from 44 Allied countries, including the Soviet Union.

16. A brief background is necessary to contextualize the negotiations around redesigning of international payments system in BW. During 1930s, Britain operated a British trading bloc with payments system known as *Sterling Area*, under which Britain's trade deficit was financed by running a financial account surplus. This outcome was conveniently achieved by requiring recipients of pounds sterling in the Empire to place their deposits in London banks. This arrangement also helped Britain to avoid recourse to debt financing of trade deficit or to implement painful adjustment policies.

17. Prior to the BW conference, both the US and UK Treasury teams spent two and a half years of planning for freer trade arrangements along with a stable international payments system. Keynes agreed with Harry White statement that *the absence of a high degree of economic collaboration among the leading nations will...inevitably result in economic warfare that will be but the prelude and instigator of military warfare on even vaster scale*. As the principal architects, both agreed on the need to stem 'beggar-thy-policy' of competitive devaluations, the need for lowering tariffs, and maintain fixed exchange rates, and tight control over speculative financial flows to facilitate smooth functioning of international trade.

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<sup>2</sup> Dow, Sheila (2018): Keynes on Domestic and International Monetary Reform; published in S. Dow, J. Jespersen and G. Tily (eds): *The General Theory and Keynes for the 21st Century*; (page 5).

<sup>3</sup> *ibid*

18. However, Harry White rejected Keynes proposals that the trade surplus countries are forced to either import from deficit countries, invest and build factories in deficit countries or transfer surplus to deficit countries. Keynes also proposed a supranational reserve currency (called *bancor*) along with the establishment of an *international clearing union* that will autonomously implement the “use-it-or-lose-it” mechanism to counteract hoarding of gold reserves by trade surplus countries. The US objected to the Keynes proposal of supranational reserve currency and, instead, requested that the US dollar be adopted as the reserve currency. The BW conference acceded to the US request.

19. The key difference between the two approaches was that White favoured a stabilization fund (i.e. IMF with adequate resources to counteract destabilizing speculative financial flows) designed to create price stability amongst the major economies while Keynes supported institutional arrangement, based on “use-it-or-lose-it” mechanism, that will assist in recovery and growth in war-torn countries.

20. There were three major reasons for US rejection of British proposal. First, between 1940 and 1950, US economic growth gyrated widely: 8.8% in 1940, 18.9% in 1942, -11.6% in 1946, and 8.7% in 1950, which, of course, reflected the vicissitudes of the war economy. Secondly, US overall goods trade surplus (as percent of GDP) increased from 1.8% in 1940 to 4% in 1950. The share of US trade surplus in manufactured goods (as percent of GDP) increased from 2% in 1940, peaked to 5% in 1945 and then fell to 2% in 1950. Thirdly, in 1944, US Federal Reserves held \$26 billion, which were two-thirds of the world’s gold reserves with the central banks (\$40 billion), which were mainly augmented by highly indebted European countries transfer of gold to the US during the inter-war period.

21. At the time of BW conference, US was also planning to participating and financing reconstruction work in war-torn countries as well as eyeing increased exports of goods and services to European and East Asian markets. US was also supporting decolonization of the British Empire to find newer markets for exports of manufactured goods. Seizing these opportunities would allow the US economy to shift and transition from a war economy to peacetime economy, to sustain economic growth momentum and achieve higher employment and prosperity. Accepting Keynes proposal would have entailed the US to accept loss of potential economic gains and erosion of its gold reserves.

22. Keynes in his speech at the closing plenary session of the BW politely noted: *We, the delegates of this Conference, Mr President, have been trying to accomplish something very difficult to accomplish...It has been our task to find a common measure, a common standard, a common rule acceptable to each and not irksome to any.* However, one senior official of the Bank of England reportedly was much forthright in his comment: *One of the reasons BW worked was that the US was clearly the most powerful country at the table and so ultimately was able to impose its will on the others, including an often-dismayed Britain. At the time, .... described the deal reached at BW as the greatest blow to Britain next to the war, largely because it underlined the way financial power had moved from UK to the US.*<sup>4</sup>

23. Eventually, the BW agreement guaranteed convertibility of national currencies within 1% of fixed parity with the US dollar which, in turn, was convertible at US\$35 per troy ounce of fine gold. IMF, which was conceived as intergovernmental institution, was established with rules to monitor movements in exchange rates, prevent competitive devaluations and lend reserve currencies to countries with balance of payments deficits. IMF was also mandated to exercise *surveillance* role (now known as Article IV consultation) of all its member countries to address persistent trade imbalances. And, in the post-BW era and without Keynes proposed autonomous

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<sup>4</sup> After the BW agreement, and given serious food shortages at the time, Britain had no choice but to seek US aid, which approved grant aid of \$4.4 billion on 6th December 1945 and then the British Parliament ratified the BW agreement in late December 1945.

“use-it-or-lose-it” mechanism, herein lies the Achilles heel of regular and major episodic international payments crises. This aspect will be covered in subsequent sections of this article.

24. Essentially, the final outcome of the BW conference reflected an epic struggle of two competing ideas as well as insidious politics between the two key players – Harry Dexter White (Assistant Secretary of US Treasury), an economist, who managed to ensure US dominance in the new international monetary order.<sup>5</sup> However, Keynes (representing UK Treasury Department), a visionary academic, lost the battle of ideas. Between the two, the final outcome also mirrored the economic and military realities of the US and UK.

## Keynes Vindication in post-BW Era

25. To manage the new international trade and payments system, the US economic and foreign aid policies in the post-BW era basically ended up validating Keynes genius proposal of autonomous “use-it-or-lose-it” mechanism tabled during the BW conference. To achieve the overall systemic trade and payments stability as well as engender economic growth and employment in trade deficit countries, Keynes plan in essence proposed that the US increases imports, invests abroad, or extends grant aid. US policies in the post-BW era ended up acting exactly along these three policy domains.<sup>6</sup>

26. Essentially, in the post-BW era, the logical imperative of the new international monetary order, based on gold-based US dollar as the international reserve currency, required the US to run increasing trade deficits. And, to finance trade deficit required an outflow of US reserves to the rest of the world, i.e. a US financial account deficit. However, in reality, the US was running large trade surpluses and accumulating reserves. Both the IMF and IBRD were not sufficiently capitalized to extend loans and meet the rising demand for US dollar, emanating particularly from Europe and East Asia. Between 1944 and 1947, the new international monetary system was failing with severe US dollar shortages in the rest of the world.

27. On 3rd April 1948, President Truman announced the launching of Economic Recovery Act (also known as Marshall Plan, amounting to \$5 billion grants that ended in December 1951) to provide large-scale grant aid for rebuilding infrastructure and to prevent sliding countries into social and political disorder in Europe. From 1950, the US deliberately ran a balance of payments deficit in order to provide US dollar liquidity to the rest of the world. Over the period 1948 to 1954, the US provided \$17 billion (adjusted for inflation, equivalent to about \$200 billion in 2025) in grant aid to 16 west European countries. In addition, the US multinationals investments abroad increased rapidly.

28. It needs to be noted that, during the BW conference, Keynes estimated that European countries would require \$10 billion of imports to rebuild their economies. Harry White rejected

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<sup>5</sup> A brief digression is in order. "The Soviet Union is a coming country; Britain is a going country:" Harry White told Keynes at one point in their long and difficult negotiations. Keynes was puzzled by White's obsession with Soviet Union and outright hostility to Britain. As it was found out later, corroborated by captured Soviet cables long before McCarthyism, White was passing government secrets to the Soviet Union. Dozens or more employees of US Treasury's Monetary Research Division, who were present in Bretton Woods, were KGB agents. President Harry Truman named Harry White as the first US Executive Director of the IMF in 1946. However, FBI Director, Edgar Hoover, submitted a report to President Truman that White was "a valuable adjunct to an underground Soviet espionage organization", which not surprisingly ended his technocratic career. Source: Sylvia Nasar (2011): *Grand Pursuit: The Story of Economic Genius*; published by Simon & Schuster (see page 396-397).

<sup>6</sup> Davidson, Paul (2011): *The Keynes Solution for Preventing Global Imbalances*; paper presented at conference "From Crisis to Growth? The Challenges of Imbalances, Debt and Limited Resources; hosted by Research Network on Macroeconomics and Macroeconomic Policies; Berlin, Germany (see page 7-8).

Keynes plan arguing that Congress would not approve \$10 billion financing of imports by European countries and indicated \$3 billion instead as the US contribution to reconstruction.<sup>7</sup>

29. Since 1950, US ran persistent overall trade deficit. As a result, for instance in 1958, Federal Reserve sold \$2 billion in gold reserves to foreign central banks.<sup>8</sup> In response, various American administrations, between 1956 to 1969, deployed use of restrictive trade policy instruments such as *voluntary export restraints* (VERs) and *import quotas*, particularly directed at the deemed Japanese export malpractices.<sup>9</sup> These instruments represent a method of discrimination against low cost, efficient producers. The application of VERs and other trade restrictions were also inconsistent with the MFN status under the GATT multilateral trading system. Nevertheless, the US actively supported Japan's accession to the GATT in 1955 in return for its cooperation in the form of export restraints to the US market.

30. For instance, some of the major restrictive US trade actions, which were primarily instituted in response to domestic protectionist requirements of US producers, are VERs on Japanese tuna (both raw and processed) under Truman; oil import quotas, detailed VERs on cotton products, plywood, sewing machines, kitchen utensils, and tuna under Eisenhower; VERs was expanded to twenty-nine major exporting and importing countries to regulate international trade in textiles under Kennedy; and the accelerated use of VERs on iron & steel, wool, polyester, glass, electronics and footwear were expanded to Japan, EEC, Korea, Taiwan, Hong Kong and other countries under Johnson and Nixon administrations.<sup>10</sup>

31. The US liberal trade policies in the post-BW era came under considerable stress from rising protectionist sentiments. Various US administrations were faced with considerable domestic political pressures to stimulate domestic employment growth by restricting imports and increasing exports.

32. The US Treasury Secretary, John Connally, under Nixon administration is reportedly to have quipped: "*foreigners are out to screw us, our job is to screw them first.*"<sup>11</sup> The Treasury Department staff economists, in May 1971, argued in an internal report that the US should "*take advantage of the present crisis to achieve (i) a lasting improvement in the balance-of-payments position of the United States, (ii) a more equitable sharing of the responsibilities for world security and economic progress, (iii) a basic reform of the international monetary system, (iv) suspension of gold convertibility, (v) imposition of trade restrictions, (vi) diplomatic and financial intervention to frustrate foreign activities which interfere with the attainment of our objectives, and (vii) reduction of the U.S. military presence in Europe and Japan.*"<sup>12</sup>

33. Today, fifty-four years later, the US and the rest of major economies are still faced with the same set of challenges of building a equitable global trade and payments system that also has the support of domestic political constituencies anchored in sustained economic growth and national employment. In 1970s and 1980s, the US was busy in *battle of wits* with Japan and Europe, today the US is engaged with China in an epic tariff and trade war.

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<sup>7</sup> *ibid* (see page 10).

<sup>8</sup> *ibid* (see page 14).

<sup>9</sup> Irwin, Douglas A. (2012): The Nixon Sock After Forty Years: The Import Surcharge Revisited; NBER Working Paper No. 17749 (see page 7).

<sup>10</sup> McClenahan, William (1991): The Growth of Voluntary Export Restraints and American Foreign Policy, 1956-1969; published in Business and Economic History, Volume 20 (see pages 182-184; 187-188).

<sup>11</sup> Irwin, Douglas A. (2012): The Nixon Sock After Forty Years: The Import Surcharge Revisited; NBER Working Paper No. 17749 (see page 8).

<sup>12</sup> *ibid*

## US as a 'Hegemon' or a 'Victim' in International Trade and Monetary System?

34. From a *realist* perspective, it is only natural for the US, it being a dominant great power, to design and shape economic, trade and payments arrangements in its national interests. Whenever such interests have been threatened, historically, various US administrations have had no compunction in changing rules or reneging on its multilateral legal commitments and agreements.

35. The first dramatic demonstration of *realist* policy action came about in the US financial crisis of 1933. As a result of significant gold outflows from Federal Reserve arising from speculative attack on gold-backed US dollar parity, President Roosevelt administration, starting from March 1933, took series of steps that suspended the gold standard; made a legal requirement to surrender gold certificates, prohibited financial institutions from converting dollar deposits into gold; reduced the gold content of the dollar by 50%; Congress abrogated gold clauses in both government and private contracts; and initiated buy-back gold program that deliberately devalued dollar against other currencies. At the time, critics termed the Roosevelt administration policies as “*completely immoral*” and “*a flagrant violation of the solemn promises made in the Gold Standard Act of 1900*”, and “*frightening and confusing consumers and businessmen*”.

36. The policy goal of Roosevelt administration drastic steps was to reinflate the economy by resuscitating banks, helping businesses to lessen debt servicing burden and to increase exports. Without delving into assessing the economic merits of policy goals, it is sufficed to note that, in the midst of Great Depression and unemployment hitting at 25% in 1933, Roosevelt administration responded to domestic political imperatives and did not hesitate to upend the legality and solemn commitments made under the trade and monetary arrangements of the time.

37. In the post-BW era, the persistent trade imbalance between the US and the rest of the world also made it difficult to maintain the parity of gold-backed US dollar, which under the BW agreement was set at \$35 an ounce. In essence, there were two parallel systems – US dollar convertibility to gold at a fixed price between central banks and open gold market. If the gap between the two rates widens significantly, then the central banks would be incentivized to convert their US dollar holdings with Federal Reserves gold and then sell it in the open market. Thus, BW system created inherent systemic instability between the need for persistent US trade deficits to provide liquidity to the rest of the world and erosion of confidence in the US dollar as the reserve currency (this conflict between short-term needs and long-term goals came to be known as *Triffin Dilemma*).

38. Again, one is reminded of Keynes genius in proposing a supranational currency as the reserve currency during the BW conference, whose adoption would have spared the US from pursuing messy distortionary industrial policies at home and restrictive trade policies abroad while, at the same time, having to deal with sustained erosion of Federal Reserve gold holdings. In 1961, London Gold Pool was established between eight governments to manage spikes in gold prices; in 1967, there was run on gold in the Sterling area and British government was forced to devalue the pound; in 1968, West Germany agreed to hold US dollar and not convert into gold while France continued to build gold reserves; in mid-March, 1968, the London Gold Pool was dissolved and, at the request of the US government, the London gold market was closed. Basically, the US government responded to various events during 1968 through a patchwork that *in effect* led to the demise of the Bretton Woods system and was converted into a combination of floating the gold peg, enforced through fiat policy and restrictions to honour transfer from foreign accounts, and repealing of 25% requirement of gold backing of the US dollar.

## Nixon's 1971 Shock Announcement and Dismantling of the BW System

39. By 1969, it was clear that the continued dollar overvaluation made the imports in the US cheaper and exports less competitive. Eventually, the various patchwork by US governments proved ineffective in maintaining BW dollar currency parity and payments system. On 13th August 1971, President Nixon secretly convened a group of carefully selected advisors in Camp David and, after two days of deliberations, formally made a shock announcement: proposed tax cuts, 90-days freeze on prices and wages, suspension of dollar convertibility into gold, and an additional 10% tariff on all dutiable imports. Basically, Nixon shock announcement was aimed at preventing a run on US gold reserves and to reverse trade deficits by 'forcing' other countries to revalue their currencies.

40. This was the second singular moment where US unilaterally announced without consultation with other western allies. But, the overall domestic US context and global monetary conditions in 1970 were far more connected than at the time of the BW conference in 1944. Unlike unilateral US actions in 1933, both BW agreement and post-Nixon announcement created new conditions and challenges for international cooperation mechanism for coping with the trade and payments realities.

41. In negotiations leading up to a new set of fixed exchange rates among ten industrialized democracies, Germany readily agreed to revalue its currency while France insisted on instituting exchange controls, dual exchange rates, and restrictive trade practices to preserve the existing parities. Japan adamantly resisted Yen revaluation and carried out massive purchase of US dollar (\$4 billion) in just two weeks of August, 1971 to maintain the Yen parity in foreign exchange market.<sup>13</sup> By the end of August, Japan gave up the fixed parity and adopted *yen dirty float* regime with regular interventions to slow its currency appreciation.<sup>14</sup> Finally, the Smithsonian Agreement was concluded on 18th December 1971. Even then, Smithsonian Agreement on new exchange rate parities also did not last long, and in February 1973, the dollar was again devalued.

42. As part of the Nixon shock announcement, the imposition of uniform 10% import tariffs was a highly popular trade restrictive measure amongst the US business associations. Nevertheless, this measure created intense internal rift between John Connally (Treasury Secretary) and Henry Kissinger (Secretary of State). Kissinger was concerned that this measure could jeopardize trans-Atlantic relationship especially in the light of planned retaliatory measures (such as Germany-France rift, Japan reluctance to correct bilateral trade imbalance, diplomatic protests by Latin American countries who were all running trade deficit with the US, Canada demanded exemption because its currency was already floating, EEC filed a complaint with the GATT, and Denmark announcement of 10% imports surcharge).<sup>15</sup> Two days later after the Smithsonian Agreement was signed, Nixon withdrew the uniform 10% import tariffs.

43. In 1992, Paul Volcker wrote an assessment on the Smithsonian Agreement and Nixon's withdrawal of uniform 10% import tariffs: "*it was well short of what we felt we needed to restore a solid equilibrium in our external payments, even if we had succeeded in opening Japanese and European markets in trade talks. But the stonewalling of the Common Market and Japan had been effective. With the exchange rate realignment settled and the import surcharge removed, we had little negotiating leverage.*" At the time, most of

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<sup>13</sup> Irwin, Douglas A. (2012): The Nixon Sock After Forty Years: The Import Surcharge Revisited; NBER Working Paper No. 17749 (see page 16).

<sup>14</sup> Apparently, one of the reasons for its reluctance was that the Japanese Finance Minister was assassinated in 1932 on account of his policies that led to a 17% revaluation of Yen.

<sup>15</sup> Irwin, Douglas A. (2012): The Nixon Sock After Forty Years: The Import Surcharge Revisited; NBER Working Paper No. 17749 (see page 19 & 22).

the leading American economists were highly critical of the uniform 10% import tariffs; terming it as *recklessly dangerous* and *bringing the world to the brink of economic war*.

44. Nixon's import tariffs also led complaints to GATT commitments as well as domestic legal challenges. Shortly after US tariff imposition, GATT, under its Article XV, established a Working Party and initiated procedurally required IMF consultation on whether or not US balance of payments conditions warranted tariff imposition. The IMF supported the US action aimed at stemming further and serious deterioration of balance of payments. However, the GATT Working Party, while taking note of IMF assessment, concluded that US tariffs constituted restrictive trade measure that placed undue and serious adjustment burden on its trading partners.

45. In February 1972, the domestic legal challenge was mounted by an importer of Japanese zippers on the grounds that the President had no legal authority and entered a plea that duties paid are reimbursed. Originally, President Nixon had declared existence of a *national emergency* and then invoked provisions of the Trading with Enemy Act of 1917 for the imposition of the uniform 10% import tariff. In July 1974, a three-panel of judges at the US Customs Court unanimously ruled in favour of the plaintiff. The US government appealed and, in November 1975, the US Court of Customs and Patent Appeals reversed the earlier Court verdict.

46. Since 1971, there have been numerous attempts by various industry lobby groups to influence the White House, Treasury and Congress to correct overvaluation of US dollar and tariff imposition (including VERs and import quotas) as measures of dealing with persistent trade deficits, especially on countries running large trade surpluses with the US. Various US administrations have been largely successful to leverage threat of domestic protectionist pressures to seek greater international cooperation. The high point of such international cooperation was the Plaza Accord of September 1985 in which an agreement was reached amongst the UK, France, West Germany, Japan and US to coordinate interventions in currency markets to engineer orderly depreciation of dollar.

## The Tale of Two Economies: America the Demand Engine, China the Manufacturing Workshop

47. In the global economic theatre, two giants—America and China—have taken on starkly contrasting roles. Over the past two decades, the United States has become the world's *engine of demand*, while China has emerged as its *workshop*. Behind these roles lie strategic choices that reflect not only divergent economic priorities, but fundamentally different philosophies on the role of the state in shaping market outcomes.

48. President Obama, in his Congressional speech in September 2011, urged the passage of a Jobs Bill that essentially endorsed the standard canard of solving jobs and payment problems via competitive free trade. President Obama said: "*The long run solution of the US unemployment problem and thereby restoring prosperity .... will rely on .... a series of trade agreements that would make it easier for American companies to sell their products in Panama, Columbia, and South Korea while helping the [American] workers whose jobs have been affected by global competition. If Americans can buy Kias and Hondais, I want the folks in South Korea driving Fords and Chevys and Chryslers. I want more products sold around the world with three proud words "Made in America."*"<sup>16</sup>

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<sup>16</sup> Davidson, Paul (2011): The Keynes Solution for Preventing Global Imbalances; paper presented at conference "From Crisis to Growth? The Challenges of Imbalances, Debt and Limited Resources; hosted by Research Network on Macroeconomics and Macroeconomic Policies; Berlin, Germany (quoted on page 3).

49. Like their predecessors, over the past two decades, every American President has launched various initiatives to *bring jobs back to America*. This is the imperative of American democracy and a hard political reality, at least over the past century. Again, it is time to invoke Keynes genius. In “*A Post War Currency Policy, 1941*”, Keynes wrote: “*to suppose [as the conventional wisdom does] that there exists some smoothly functioning automatic [free market] mechanism of adjustment which preserves equilibrium if only we trust to methods of laissez-faire is a doctrinaire delusion which disregards the lessons of historical experience without having behind it the support of sound theory.*”

50. The hard fact is this: the economic stimuli implemented by recent U.S. administrations—whether in response to global or domestic financial crises, pandemics, or inflationary shocks—have done more than just stabilize domestic markets. They’ve functioned as a *global demand boost*, pouring liquidity into the economy and fuelling consumption at scale. American households, flush with stimulus checks and buoyed by easy credit, have kept the engines of global trade humming—mostly by importing what the rest of the world is eager to supply.

51. China, by contrast, has managed its economy with a cool pragmatism. Consumer spending remains a growing but deliberately restrained component of its aggregate demand. Instead, *China has prioritized investment, production, and export-led growth*, consolidating its status as the manufacturing backbone of the global economy. While U.S. consumers absorb goods, Chinese factories produce them—at a scale and efficiency unmatched anywhere else.

52. According to the U.S. Bureau of Economic Analysis (BEA), personal consumption expenditures in 2023 were approximately \$18.2 trillion, which is more than double the combined spending of all EU nations and accounted for 34% of the world's household consumption in 2022. US retail sales increased from \$3 trillion in 2000 to more than \$7.2 trillion in 2023. In 2010, the US trade balance was a deficit of \$498 billion (-2.8%GDP); in 2015, the trade balance posted a deficit of \$526.199 billion (-2.9% of GDP); in 2020, the deficit reached \$626.39 billion (-2.9% of GDP) and by 2023, the deficit was \$953.7 billion (-3.0%GDP).

53. In 2023, China's consumer spending reached a record \$7.1 trillion while retail sales are estimated at \$6.79 trillion. In contrast, in 2010, China had a trade surplus of \$181.76 billion (27.2% of GDP); by 2015, the trade balance had increased to \$593.902 billion (21.4% of GDP); in 2020, the trade balance reached \$355.15 billion (18.6% of GDP); and in 2023, China's trade balance was \$822.69 billion (19.7% of GDP). Quite clearly, China’s manufacturing capacity is outpacing domestic demand and leading to significant trade imbalances globally.

54. In 2023, China ran a bilateral trade surplus with an astonishing 150 out of 181 countries. The handful of exceptions—just 31 nations—were mostly rich in natural resources.<sup>17</sup> This is not mere trade efficiency; it’s a structural dominance or is it growth immiseration or income impoverishment on a global scale? One suspects that Keynes would have been appalled. The scale of China’s accumulation of foreign exchange reserves amounts to a kind of global hoarding—precisely the imbalance Keynes sought to prevent when he warned against nations perpetually exporting more than they import.

55. This division of role in global economic system has produced an alarming asymmetry: in both countries, there is a *hiatus between domestic consumption and trade balances*. The U.S. runs persistent trade deficits while maintaining high consumption. China posts regular trade surpluses despite relatively modest household spending. This split reflects deeper structural choices—and exposes the limitations of neoliberal economic orthodoxy.<sup>18</sup> After the 1971 Nixon shock, the

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<sup>17</sup> Matthes, Jürgen (2024): China’s Trade Surplus – Implications for the World and for Europe; Intereconomics; Review of European Economic Policy; Vol. 59, 2024.

<sup>18</sup> The standard neoliberal orthodoxy for resolving trade imbalances can be best illustrated by contextualizing with reference to Eurozone crisis, which started in 2010. Since Germany was running trade surplus, there must be corresponding trade deficit in some Eurozone countries, such as Greece, Portugal and Ireland. Such trade deficit

gradual emergence of new neoliberal economic governance across the world did not function to strengthen social democracies; rather, it set out to extend markets while limiting the way states could intervene in them.

56. Behind the hiatus lies the fact that *financial capitalism* in western countries started to gradually dominate the *industrial capitalism*, which Keynes had warned against in his writings during the inter-war period. After China joined WTO in December 2001, the US led in shifting of industrial base to China – the outsourcing of production was essentially outsourcing of profits while the industrial workers faced job losses and stagnant wages. Since the late 1970s, U.S. and European companies have significantly increased their foreign direct investment (FDI) in China, aligning with China's economic reforms and opening to global markets.

57. U.S. overseas investments began modestly in the early 1980s, with actual FDI rising from approximately \$1.8 billion between 1979 and 1982 to \$4.86 billion by 2001. By 2016, the cumulative U.S. FDI stock in China reached \$92.5 billion, making China the 12th largest destination for U.S. FDI at that time. In 2023, North American countries, including the U.S., accounted for 2.4% of China's total actual utilized FDI, indicating a relative decline in share compared to earlier years.<sup>19</sup> European investment, particularly from Germany, has shown resilience and growth. In the first half of 2024, German FDI constituted 57% of total EU investments in China, driven largely by the automotive sector. EU greenfield investments reached a record €3.6 billion in the second quarter of 2024, highlighting a strategic push to localize production amidst global economic shifts.<sup>20</sup>

58. Overall, while U.S. FDI in China has seen fluctuations and a relative decline in recent years, European, especially German, investments have maintained a strong presence, adapting to China's evolving economic landscape. FDI has played a significant role in China's export sector, particularly during the early stages of its economic reform. In the early 2000s, FDI accounted for approximately 61% of exports in labour-intensive industries such as garments and footwear. This high percentage indicates that foreign-invested enterprises were instrumental in driving China's export growth during that period.<sup>21</sup>

59. However, over the years, the proportion of exports attributed to foreign-invested enterprises has declined. By 2023, these enterprises contributed to about 28.6% of China's total export value, down from a peak of 58.3% in 2005. This trend reflects China's evolving economic landscape, where domestic firms have become more prominent in the export market, and the country has shifted towards higher value-added production and services.<sup>22</sup>

60. Offshoring FDI to China has had a significant impact on employment and labour incomes in the United States and Europe, particularly in the manufacturing sector.<sup>23</sup> Between

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countries must achieve a new level of competitiveness by reducing their labour costs and increasing productivity relative to Germany's labour costs and productivity. These trade deficit countries will then be able to expand their exports to other Euro partner countries. At the same time, Germany must also become relatively less competitive and lose shares in both domestic and export markets. Source: Davidson, Paul (2011): *The Keynes Solution for Preventing Global Imbalances*; paper presented at conference "From Crisis to Growth? The Challenges of Imbalances, Debt and Limited Resources"; hosted by Research Network on Macroeconomics and Macroeconomic Policies; Berlin, Germany.

<sup>19</sup> China Briefing: China's FDI Trends 2024: Key Sources, Destinations, and Sectors (6th November 2024).

<sup>20</sup> Rhodium Group: Don't Stop Believing: The Inexorable Rise of German FDI in China (31st October 2024).

<sup>21</sup> IMF eLibrary: IMF Economic Forum: For China, foreign direct investment translates into higher productivity growth (1st January 2002).

<sup>22</sup> Textor, C: Foreign invested companies' share in total import and export in China 1986-2023 (published by Statista, 18th November 2024).

<sup>23</sup> Robert, E. Scott and Zane Mokhiber: Growing China trade deficit cost 3.7 million American jobs between 2001 and 2018, Jobs lost in every U.S. state and congressional district; Economic Policy Institute (30th January 2020). For the same period, EPI research paper presents estimates of net jobs displaced in both non-manufacturing and

2001 and 2018, the growing U.S. trade deficit with China led to the displacement of approximately 3.7 million American jobs, with about 75% of these losses occurring in manufacturing industries such as electronics, textiles, and furniture. The phenomenon known as the "China shock" resulted in higher unemployment, reduced labour force participation, and wage stagnation in regions heavily reliant on manufacturing. Workers displaced by trade with China often faced significant wage reductions upon reemployment, with average weekly earnings decreasing by 17.5%.<sup>24</sup>

61. In Europe, the offshoring of FDI to China has similarly affected employment and wages, though the impact varies across countries. Germany, for instance, experienced job losses in certain manufacturing sectors due to increased import competition from China. However, comprehensive data quantifying the exact number of jobs displaced in Europe due to offshoring to China is limited. Overall, the offshoring of FDI to China has contributed to job displacement and wage pressures in both the U.S. and Europe, particularly affecting workers in manufacturing and related industries.

62. Whereas the U.S. leans on trusting in financial capitalism to allocate resources (with government interventions as a crisis tool), China has never subscribed to such orthodoxy. Despite its embrace of market reforms, China's economy remains state-guided at its core. Chinese state wields control where it deems necessary from steering credit, setting industrial priorities, and protecting strategic sectors. In truth, the Chinese model avoids what Keynes best described as *doctrinaire laissez-faire delusions*. It prizes results over rhetoric, control over chaos, and planning over platitudes. That may not sit well with neoliberal economists, but the question is: has it delivered decades of sustained growth, macroeconomic stability, industrial strength, and reducing income inequality?

63. As the world navigates a new phase of economic realignment—marked by reshoring, protectionism, and technological decoupling—its worth asking which approach offers more resilience. The U.S. is the engine of global consumption, but China has built the factory that keeps the machine running. The contrast could not be more revealing. Will the pragmatic western politicians heed the advice of Mariana Mazzucato in her three books – *The Entrepreneurial State; The Value of Everything; and The Mission Economy* – of building (*capable*) public and fostering (*innovative & risking taking*) private partnership in value creation and market shaping?<sup>25</sup>

## Has the IMF Been Sleeping at the Wheels of Global Imbalances?

64. IMF was created to promote international monetary cooperation, facilitate balanced growth of international trade, and ensure exchange rate stability. In principle, IMF is mandated

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manufacturing sectors. In particular, in the 'finance and insurance' sector, the net jobs loss is estimated at -51,600. Furthermore, estimates of jobs losses by State and Congressional districts are also provided.

<sup>24</sup> China also experienced job losses in its manufacturing sector that are mainly caused by structural shifts in the labour market and supply chain disruptions due to spread of 2020 COVID and 2023 Omicron viruses. Behind its international competitiveness, China experienced major productivity gains and undertook SOEs industrial restructuring which, between 1995 and 2002, led to 15 million manufacturing job losses with negative job growth in 26 of 38 major industries (Source: McGuckin, Robert & Matthew Spiegelman (2004): Restructuring China's Industrial Sector: Productivity and Jobs in China; National Bureau of Statistics of China Working Paper Series Vol. 2004-13; July). Between 2015 and 2017, employment in broad manufacturing in China shrank by 23 million and additionally jobs lost were 5 million in 2018 alone (Source: Lardy, Nicholas (2019): China's Manufacturing Job Losses Are Not What They Seem; Peterson Institute for International Economics; August).

<sup>25</sup> Mazzucato, M. (2025). Principles for an inclusive and sustainable global economy: A discussion paper for the G20. UCL Institute for Innovation and Public Purpose. Available at: <https://www.ucl.ac.uk/bartlett/ucl-institute-innovation-and-public-purpose/principles-inclusive-and-sustainable-economydiscussion-paper-g20>

to operate as a cooperative institution where member countries collectively oversee and adhere to a code of conduct governing monetary and financial policies. This cooperative framework is central to the IMF's identity, emphasizing surveillance and policy coordination to maintain global economic stability.

65. Surveillance is IMF's core functions and institution's central activity.<sup>26</sup> Through surveillance, the IMF monitors member countries' economic and financial policies, providing assessments and recommendations to promote stability and prevent crises. Over the decades, IMF's surveillance function has formally evolved in the direction of bilateral, Article VIII consultation. IMF's surveillance mandate followed the Second Amendment to its Articles of Agreement in 1978. The amendment introduced "*firm surveillance*" over exchange rate policies, allowing countries to adopt floating or managed exchange rates instead of fixed par values. This shift aimed to ensure systemic stability while avoiding manipulation of exchange rates for competitive advantage.

66. The IMF's surveillance mandate was divided into *bilateral surveillance*, focusing on individual members' exchange rate policies, and *multilateral surveillance*, overseeing the international monetary system. The 1977 Decision established general principles for bilateral surveillance, but these were vague, reflecting divergent views among member countries. The Decision listed five conditions that might indicate the need for discussions with a member, such as protracted intervention in exchange markets or unsustainable borrowing.

67. The IMF faced challenges in implementing its *bilateral surveillance* mandate due to the subjective nature of assessing exchange rate policies and economic conditions. The ambiguity of terms like "*protracted intervention*" and "*balance of payments purposes*" made it difficult to enforce the mandate effectively. While the 1977 Decision aimed to provide a framework for *bilateral surveillance*, its vague language and reliance on subjective assessments hindered its practical application. The IMF's efforts to exercise *firm surveillance* were further complicated by differing views among member countries on the goals of exchange rate stability versus market-driven adjustments. As a result, the IMF's ability to oversee exchange rate policies and ensure global systemic stability among major economies remained constrained, highlighting the need for clearer guidelines and more effective tools for surveillance.

68. IMF's *multilateral surveillance* role evolved with informal engagement with the G7, starting in the 1980s. The Second Amendment to the Articles of Agreement tasked the IMF with overseeing the international monetary system, but major industrial countries like the G7 began assuming informal oversight roles. In 1982, the G7 Summit issued a communiqué emphasizing their commitment to monetary stability and collaboration with the IMF. The IMF supported this *multilateral surveillance* process by providing technical advice, but its role was informal and not subject to Executive Board approval. The IMF Managing Director participated in G7 meetings in a personal capacity, sharing IMF assessments without presenting official views. This informal arrangement allowed the IMF to assist the G7 while maintaining confidentiality, but it also raised questions about the Fund's mandate and governance.

69. By mid-1980s, the effectiveness of IMF *multilateral surveillance* was widely criticized, particularly due to its inability to address large swings in major-currency exchange rates. Both the G10 and G24 called for refinements to make surveillance more even-handed and effective. In response, the IMF's 1986 biennial surveillance review proposed adopting more specific indicators, such as reference ranges for exchange rates and medium-term economic targets, to strengthen its oversight. While the Executive Board allowed the staff to experiment with these ideas, it did not amend the 1977 Surveillance Decision. However, the lack of formal changes

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<sup>26</sup> Boughton, James M.: Interpreting and Amending the IMF Mandate, 1944-2011; Independent Evaluation Office, IMF (May 2024). This Section mainly relies on insights gleaned from this document.

highlighted challenges in achieving consensus and effectively addressing global systemic instability. Nevertheless, the *analytical* scope of multilateral surveillance was broadened to cover areas of *policy interdependence* among the major economies which also got annually reported in the *World Economic Outlook* and *Global Financial Stability Report*.

70. The US has long criticized IMF for turning a blind eye to the persistent and politically charged trade imbalances between China and the United States, effectively "*sleeping at the wheel*" while one of the most consequential economic tensions of our time festered. Despite its mandate to promote global economic stability and oversee exchange rate policies, the Fund has consistently sidestepped taking a firm position on China's currency practices or the structural causes behind its massive trade surpluses. Instead of acting as an impartial arbiter, the IMF has often appeared constrained—probably under the influence of diplomatic caution—failing to hold China meaningfully accountable for policies that contributed to persistent global imbalances, while also neglecting the U.S. side of the equation. This hesitancy has undermined its credibility as a global watchdog and left one of the most critical fault lines in the international monetary system largely unaddressed.

## Assessment of IMF's Multilateral Surveillance Work

71. The IMF's 2012 *Spillover Report* and *Pilot External Sector Report* mark an evolution in the Fund's multilateral surveillance efforts to focus attention on implications of persistent global imbalances.<sup>27</sup> The *Spillover Report* examines how policies in five major economies—China, the Eurozone, Japan, the UK, and the US—affect the global economy, identifying key risks such as euro area instability, U.S. fiscal and monetary policies, Chinese economic shifts, and Japanese fiscal issues. Meanwhile, the *External Sector Report* (ESR) introduced a new model for assessing "external balance," using the IMF's own judgment to determine which global imbalances are acceptable or distortive. These reports were introduced as part of the IMF's Integrated Surveillance Framework, aiming to enhance multilateral surveillance by providing an in-depth assessment of the external positions of the world's largest economies. The ESR reports offers a comprehensive assessment of the external positions of major economies, integrating both multilateral and country-specific analyses to ensure a coherent and globally consistent perspective. External assessments are derived through a combination of the External Balance Assessment (EBA) methodology, country-specific evidence, and professional judgment, while also recognizing the inherent uncertainties associated with such evaluations.

72. The structure of the ESR report comprises three core chapters.<sup>28</sup> The first provides a multilateral overview, examining how individual economies interact within the broader global context and outlining policy recommendations aimed at reducing excessive external imbalances. The second chapter presents analytical insights into key issues relevant to external sector dynamics and the mechanisms of external adjustment. The final chapter delivers detailed assessments of the external positions of the thirty economies under review. This structure facilitates a nuanced understanding and drivers of global external imbalances and informs policy responses tailored to both national and international contexts.

73. The 2024 IMF "External Sector Report (ESR) – Imbalances Receding" is a display of impressive technical diagnostics work and computational processing of big data. The 2024 ESR underscores the imperative of addressing excess current account imbalances, which, if left unchecked, can signal inefficient resource allocation and heighten vulnerabilities to abrupt capital

<sup>27</sup> Bretton Woods Project: Revamped IMF surveillance: lacks influence? (October 2012).

<sup>28</sup> It is puzzling why ESRs are not properly titled as, for instance, *IMF Multilateral Surveillance Report on Global Imbalances*.

flow reversals. Such imbalances may also erode support for multilateralism, potentially exacerbating geoeconomic fragmentation and prompting the erection of trade barriers. To mitigate these risks, the 2024 ESR advocates for coordinated policy interventions from both surplus and deficit economies. This includes maintaining global financial system liquidity to navigate asynchronous monetary policies and geopolitical tensions, thereby enabling economies susceptible to external shocks to effectively utilize the global financial safety net.

74. Policy recommendations are tailored to the specific external positions of individual economies. For countries with *weaker-than-warranted external positions*, the emphasis is on implementing credible fiscal consolidation to reduce public debt, enhancing competitiveness through structural reforms, and safeguarding critical investments in infrastructure and social sectors. Conversely, economies with *stronger-than-warranted external positions* are encouraged to stimulate investment and reduce excessive savings, thereby supporting both domestic objectives and external rebalancing. This may involve increasing public investment in areas such as green transitions, digitalization, and healthcare. Economies with external positions broadly aligned with fundamentals should continue addressing domestic imbalances to prevent the emergence of excessive external disparities. This includes advancing market-based structural reforms, strengthening social protection systems to reduce high household savings, and enhancing exchange rate flexibility to better absorb external shocks.

75. From the perspective of Keynes's Bretton Woods proposal, which emphasized symmetric adjustment mechanisms to address global imbalances, the IMF's 2024 ESR reflects a partial, though important, commitment to global rebalancing. Keynes envisioned a system where both surplus and deficit countries would share responsibility for correcting imbalances, with a central mechanism—such as an International Clearing Union—to discipline surplus accumulation. The 2024 ESR acknowledges this principle by calling for coordinated policy responses from both groups of countries. It highlights the dangers of unchecked imbalances, including inefficient global resource allocation and rising protectionism. The report supports maintaining global liquidity and emphasizes the importance of multilateral financial safety nets, aligning with Keynes's vision of an institutional framework capable of absorbing asymmetric shocks and supporting global stability.

76. However, the 2024 ESR recommendations continue to place *disproportionate adjustment burdens* on deficit economies, echoing longstanding critiques of the post-Bretton Woods order. For countries with *weaker-than-warranted external positions*, the focus remains on fiscal consolidation and competitiveness-enhancing reforms—measures that may deepen contractionary pressures. By contrast, surplus countries are advised to stimulate investment and reduce excess savings, but these recommendations lack enforceability and urgency. This asymmetry stands in contrast to Keynes's insistence that persistent surpluses are as destabilizing as deficits and should be subject to systemic discipline. Furthermore, the absence of a global mechanism to compel adjustment by surplus countries—akin to Keynes's proposed *bancor* system—limits the effectiveness of the IMF's approach. Thus, while the 2024 ESR moves toward a more balanced framework, it still falls short of the symmetrical global adjustment system that Keynes originally envisioned.

77. Another important criticism of ESRs is their lack of efficacy in producing desired outcomes. The ESRs are reviewed by the IMF Board of Executive Directors; the minutes of Board reviews are also published. The Board reviews are mostly *polite summary* of ESRs with *some* Board members urging countries to act upon policy recommendations. In fact, the minutes of the IMF Board meeting demonstrates the political reluctance of powerful nations to implement globally beneficial policies. Essentially, the IMF's timid mechanism lacks three essential features:

*dispute resolution mandate* over monetary and financial policies, *enforcement power* and the *neutrality* required to hold deviant countries accountable.<sup>29</sup>

78. The global economic instability precipitated by the Trump administration’s imposition of *Liberation Day* tariffs—and the ensuing disruptions across business activity, financial markets, and currency exchanges—highlights, at the minimum, an urgent need for procedural reforms aimed at addressing persistent trade imbalances. These imbalances are often rooted in the strategic deployment of industrial policies and exchange rate management by surplus economies. As a potential procedural innovation, the IMF Executive Board could, drawing upon findings from the External Sector Report (ESR), develop a **time-bound Policy Coordination Action Matrix**. This matrix would consolidate policy recommendations for both countries with weaker-than-warranted and stronger-than-warranted external positions. The matrix would then be submitted to the G20 Finance Ministers and Central Bank Governors as a basis for deliberation and consensus-building.

79. These coordinated policy actions could, in turn, inform commitments at the G20 Leaders’ Summit. Such a procedural innovation would serve to **strengthen cooperative multilateralism** by shifting the implementation of actionable policy coordination from the closed deliberations of the IMF Executive Board to a more transparent and politically accountable **public and political economy arena**. By embedding external sector adjustment efforts within the broader G20 policy process, this approach enhances the legitimacy, visibility, and potential efficacy of multilateral coordination in addressing global imbalances.

## Bilateral Surveillance by the IMF: Assessments of China and the United States

80. At this stage, it will be highly instructive to examine how IMF has actually carried out *bilateral surveillance* activities with regard to China and US economies. Despite its growing clout in the global economy, China hasn’t fully accepted Article VIII obligations, especially around full currency convertibility. While China allows convertibility for trade-related payments, it continues to impose tight controls on capital flows and the renminbi’s exchange rate. These restrictions give Chinese authorities powerful tools to manage financial stability and shield the economy from volatile global markets. But by holding back from full compliance, China sidesteps the very rules designed to ensure a level playing field with respect to its other major trading partners.

81. Unlike China, the United States has fully accepted Article VIII of the IMF Articles of Agreement. This means the U.S. is already committed to avoiding exchange restrictions, discriminatory currency practices, and restrictions on current account transactions. Since the U.S. is already in compliance, the IMF doesn’t conduct separate Article VIII consultations. Instead, any issues related to exchange policies or currency convertibility are reviewed as part of the regular Article IV consultation. In other words, once a country accepts Article VIII obligations, the IMF doesn’t conduct a separate consultation just for that. It assumes compliance unless violations are observed, and any concerns are bundled into the regular surveillance that happens under Article IV.

82. The IMF’s 2024 Article IV consultation with China<sup>30</sup> deserves credit for its unusually candid tone and broad assessment of the country’s macroeconomic and industrial landscape. In

<sup>29</sup> *ibid*

<sup>30</sup> IMF Staff Report for the 2024 Article IV Consultation with People’s Republic of China (1st July 2024; see pages 34, 35 and 40).

a departure from past diplomatic caution, the report urged China to shift its growth model toward domestic consumption and greater openness in the services sector to foster sustainable growth and employment. Notably, the Fund highlighted the opaque use of industrial policies—ranging from preferential credit and direct subsidies to research grants, tax incentives, and export restrictions on critical minerals—as contributing to global uncertainty. It warned that the risks of reshoring and escalating geoeconomic fragmentation could have serious implications for China's economy. Yet, the report also fell short of a deeper dive into the data and sectoral scope of these policies, a gap likely tied to China's reluctance to provide granular information. The Chinese authorities, for their part, pushed back strongly—defending export controls as national security measures, rejecting concerns over industrial overcapacity, and attributing the global competitiveness of their firms to innovation rather than state support.

83. Meanwhile, the United States, having fully accepted Article VIII obligations, is reviewed solely through its annual Article IV consultations<sup>31</sup>. The IMF's 2023 report on the U.S. pulled few punches either, flagging that sweeping Keynesian-type policy packages—like the Inflation Reduction Act, the CHIPS Act, and Buy America provisions—risk distorting trade and fragmenting the global economic system. Instead, the Fund recommended investment in productivity, skills, and infrastructure as a better route to competitiveness. It warned against the weaponization of trade policy and urged the U.S. to pursue constructive engagement with trading partners. The US authorities responded to IMF's assessment by outlining its “*targeted industrial and innovation strategy, ... This strategy may help reverse the hollowing out of the U.S. industrial base and counter unfair subsidies by non-market economies*” and emphasizing national security, clean energy, and resilient supply chains while aligning with allies. Initiatives like the Indo-Pacific Economic Framework and WTO reform, U.S. officials claimed, are intended not to isolate, but to modernize global trade and promote sustainability, labour standards, and digital trust.

84. After Trump's administration declaration of Liberation Day tariffs, whether these competing visions for industrial policy can coexist without deepening trade warfare has now become existential challenge for global economic stability. Yet, it is also now abundantly obvious that the IMF failed to discharge its *multilateral surveillance mandate*, however weak or tentative, to influence and mobilize high-level international forums, such as G20, to develop a roadmap and mechanism for resolving trade imbalances and harmonizing industrial policies amongst the major global economies.

## Has the Moment of 21st Century Bretton Woods 2.0 Arrived?

85. In the wake of the 2008 financial meltdown, the United Nations stepped into a conversation long dominated by the IMF and World Bank. Under the leadership of Nobel laureate Joseph Stiglitz, the UN General Assembly launched a bold initiative—the *Commission of Experts on Reforms of the International Monetary and Financial System* in October 2008. This marked the first formal post-BW attempt to reimagine the global financial architecture with a sharper focus on fairness and resilience. The resulting “Stiglitz Report” didn't shy away from challenging the status quo. Among its most compelling recommendations was the creation of a global reserve system—an alternative to the current ad-hoc hoarding of foreign reserves by individual nations. The Commission argued that such a system could help smooth out economic shocks, promote greater stability, and distribute financial resources more equitably. In a world still reeling from the consequences of a deeply flawed system, the UN's message was clear: as a global public good, there was urgent need to reorder international monetary order.

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<sup>31</sup> IMF Staff 2023 Article IV Consultation Report with the United States (June 2023, see page 29 & 30).

86. In the light of rising geopolitical tensions and economic disruptions, U.S. leaders have increasingly invoked the legacy of the Bretton Woods system as both inspiration and justification for overhauling the current international economic order.<sup>32</sup> For instance, (former) Treasury Secretary Janet Yellen and (former) Trade Representative Katherine Tai have drawn on the historical narrative of Bretton Woods to argue for renewed multilateral cooperation and a redefinition of the state's economic role. Yellen, for instance, linked the original Bretton Woods moment to a broader capacity for peace and stability, especially in response to crises like the war in Ukraine. Tai, referencing the 1941 Atlantic Charter that preceded Bretton Woods, advocated for a global economic system that supports stronger labour protections and social welfare, aligning with a broader vision of economic justice.

87. Jake Sullivan (former National Security Advisor) echoed these sentiments by framing the Biden administration's economic policy as a return to the foundational values of Bretton Woods. He emphasized repairing the cracks in the global economic order by embedding national security and equitable prosperity into international financial governance. Sullivan, like Yellen and Tai, argued that the restructured global economic framework should not only bolster U.S. interests but also enable a more balanced and inclusive form of international cooperation. This approach, according to the Biden administration officials, would create a more resilient multilateral system that addresses contemporary challenges such as climate change, technological transformation, and inequality.

88. Recently, current Treasury Secretary Scott Bessent reflected on the original mission of the Bretton Woods institutions, emphasizing that the IMF and World Bank were established to foster global economic stability through coordination and the alignment of national policies with a rules-based international order.<sup>33</sup> While acknowledging their historical significance, Bessent contended that these institutions have deviated from their core mandates due to "mission creep".

89. Reaffirming the need for institutional realignment, Bessent called for a return to the founding principles of restoring global balance, particularly in trade and monetary cooperation. The Trump administration's perspective centres on the belief that "*Intentional policy choices by other countries have hollowed out America's manufacturing sector and undermined our critical supply chains, putting our national and economic security at risk. President Trump has taken strong action to address these imbalances and the negative impacts they have on Americans.*" Incidentally, this framing conveniently overlooks the United States' longstanding reliance on *financial capitalism* and the offshoring of manufacturing to China—structural shifts that have played a central role in the erosion or *hollowing* of industrial capacity, jobs losses, and the stagnation of real wages.<sup>34</sup>

90. Bessent went on to critique the IMF's approach to global imbalances, arguing that the institution has become hesitant to confront surplus economies and opaque currency practices. He stressed that the IMF needs to function as a "*brutal truth-teller*" by prioritizing macroeconomic surveillance and balance of payments stability over auxiliary agendas. Additionally, the speech advocated for a recalibration of IMF lending practices—emphasizing conditionality, transparency, and temporariness. Emphasizing America First not as isolationism but as a renewed commitment to multilateral leadership, Bessent argued that the new approach requires

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<sup>32</sup> Hamilton, Matthew: What Is Bretton Woods? The Contested Pasts and Potential Futures of International Economic Order; Carnegie Endowment for International Peace, (22nd October 2024). This Section relies on insights gleaned from this source.

<sup>33</sup> Treasury Secretary Scott Bessent Remarks before the Institute of International Finance; delivered on 23rd April 2025; <https://home.treasury.gov/news/press-releases/sb0094>

<sup>34</sup> "Americans Will Always Do the Right Thing — After Exhausting All the Alternatives", an apocryphal statement attributed to Winston Churchill; Source: <https://quoteinvestigator.com/2012/11/11/exhaust-alternatives/>

symmetry, reform, and rigorous enforcement of core mandates, rather than the preservation of a status quo marked by imbalance and inaction.<sup>35</sup>

91. However, perspectives on Bretton Woods diverge globally. While international leaders like UN Secretary-General António Guterres and IMF Managing Director Kristalina Georgieva have similarly called for a "new Bretton Woods moment," not everyone share this reverence. A report from the Chinese Communist Party rejects the need for a revival, portraying the original Bretton Woods system as a vehicle for western dominance. Instead, it advocates for an alternative model rooted in national sovereignty and economic self-determination. These contrasting interpretations reflect deeper global disagreements about how to reform international economic governance, whether to build upon the postwar legacy or replace it altogether. As the debate intensifies, historical narratives surrounding Bretton Woods continue to influence the direction and scope of possible reforms.

## Trump's Trade Warfare: Strategic Rivalry, Systemic Imbalances, and the Keynesian Echo

92. The Trump administration's imposition of tariffs on Chinese imports represents not an aberration but a continuation of a long-standing U.S. strategy of reshaping global trade rules to serve national interests. While the tariffs were in violation of WTO principles, they illuminate a deeper systemic failure that Keynes foresaw during the Bretton Woods negotiations of 1944. Keynes argued that the sustainability of a global free trade regime depended on symmetrical adjustment mechanisms between surplus and deficit countries. Without such mechanisms, persistent trade imbalances would trigger economic distress in deficit nations, leading inevitably to political backlash and protectionist responses—exactly the trajectory the global trading system now confronts.

93. The contemporary trade imbalance between the United States and China is a case in point. China's structural surpluses are matched by U.S. deficits, creating destabilizing feedback loops within both economies. In the United States, these deficits have fuelled populist resentment and scepticism toward globalization, while in China, the surpluses reinforce an economic model reliant on export-led growth and insulate domestic industries from needed reforms. Neither the WTO nor the IMF has effectively addressed political economy interdependence arising from persistent trade imbalances. The revival of unilateralism underscores a deeper structural failure long diagnosed by Keynes: a global economic system that rewards surplus countries while imposing adjustment costs on deficit economies is inherently unsustainable and politically combustible.

94. The asymmetry of adjustment mechanisms is exemplified in the U.S.–China economic relationship. As China continues to run persistent trade surpluses and maintain industrial policies that distort global markets, the United States bears the brunt of rising deficits, deindustrialization

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<sup>35</sup> Writing in FT, Prof Barry Eichengreen alerted that Trump's administration Treasury Secretary Bessent is examining the possibility of converting 5-year and 10-year Treasury bonds held by foreign investors into 100-year bonds with low interest rates. Another option being examined is taxing foreign investors of US treasuries as a way of depreciating the dollar and boosting competitiveness of US exports. According to Congressional Budget Office's estimates, US public debt is projected to rise from 99% of GDP in 2024 to 116% in 2034. Going by the past record, as the debt servicing becomes onerous, US will, once again, have no compunction in renegeing on its sovereign commitments. Along with weaponisation of dollar-based international payments system, Eichengreen points out that endless tax cuts, mythical expenditure reductions and political polarisation will seriously erode the US dollar status as a reserve currency. Source: Barry Eichengreen: Can the dollar remain king of currencies? Financial Times, 22nd March 2025.

and job losses, and supply chain vulnerabilities. Reports such as those by Foreign Affairs,<sup>36</sup> Bloomberg,<sup>37</sup> and the New York Times<sup>38</sup> suggest that China has developed “*escalation dominance*,” using its economic leverage—including export controls and retaliatory tariffs—to outmanoeuvre U.S. pressure tactics. At the same time, China is signalling its readiness to retaliate against U.S.-aligned nations, raising the stakes in a broader geopolitical contest.<sup>39</sup> This strategic interdependence complicates conventional trade conflict resolution and renders WTO arbitration largely symbolic, as it lacks both enforcement capacity and relevance in a multipolar world order.

95. Trump’s effort to construct an anti-China trade coalition marks a strategic pivot toward an allied scale framework. Rather than relying solely on unilateral tariffs, the U.S. now seeks to coordinate with like-minded nations to constrain China’s market power. However, such efforts are not without risk. Without a coherent multilateralism, these alliances may prove fragile, and the burden of confrontation could fall unevenly on Global South. Moreover, China’s retaliatory actions demonstrate its willingness to weaponize trade dependencies, with potentially severe repercussions for global supply chains and developing economies, which now face increased exposure due to market dumping.<sup>40</sup>

96. These evolving dynamics expose the inadequacies of current multilateral institutions. The WTO’s dispute resolution process is too slow and politically constrained, while the IMF remains largely passive in its surveillance of structural surpluses and unsustainable debt practices. The ambiguity over whether trade imbalances constitute a trade or macroeconomic issue has left surplus countries unaccountable. The lack of coordination between the IMF and WTO has allowed imbalances to become entrenched, undermining the credibility of global governance. A reform agenda must include giving real authority to international institutions to compel surplus adjustment, enhance debt transparency, and enforce symmetry in obligations across both surplus and deficit countries.

97. Undoubtedly, Trump’s tariffs have been economically disruptive and politically divisive, but they exposed systemic failures that can no longer be ignored. As Keynes warned at Bretton Woods, a rules-based system without mechanisms for symmetric adjustment invites not only economic inefficiency but political instability. The challenge ahead is not to return to a nostalgic version of globalization but to reimagine institutions capable of managing twenty-first-century economic power symmetries in a multi-polar world.

98. Unless reform efforts directly confront these structural deficiencies—through coordinated investment, strengthened domestic policy buffers, and enforceable multilateral frameworks—the recurring cycle of persistent trade imbalances, backlash, and renegotiation will endure. In such a scenario, Keynes’s enduring observation—that “*the political problem of mankind [is] how to combine three things: economic efficiency, social justice, and individual liberty*”—will remain an unresolved challenge at the heart of the international economic order.

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<sup>36</sup> Posen, Adam (2025): Trade Wars Easy to Lose: Beijing Has Escalation Dominance in the U.S.-China Tariff Fight; Foreign Affairs magazine, <https://www.foreignaffairs.com/united-states/tariffs-trade-wars-are-easy-lose>

<sup>37</sup> US-China: Trump Plans to Box-in China by Recruiting Other Trade Partners – Bloomberg <https://www.bloomberg.com/news/articles/2025-04-16/us-looks-to-box-in-china-by-recruiting-other-trading-partners>

<sup>38</sup> Bradsher, Keith (2025): Beijing Suspends Exporting Goods World Relies on, Escalation Hits Tech and Auto Industries and the Military, New York Times, 15th April 2025.

<sup>39</sup> China to retaliate against nations that work with U.S. to isolate Beijing <https://www.cnbc.com/2025/04/21/china-to-retaliate-against-nations-that-work-with-us-to-isolate-beijing.html>

<sup>40</sup> BBC (2025): Trump’s tariffs leave China’s neighbors with an impossible choice, 19th April 2025 <https://www.bbc.com/news/articles/c0455k6g71eo>

## Conclusion and Forward Pathways

99. The contemporary global economic landscape is marked by an unprecedented degree of complexity, where economic interdependence, demographic transitions, and geopolitical fragmentation intersect. Unlike the more contained postwar environment, stability and prosperity today require a delicate recalibration of economic efficiency, supply chain resilience, and strategic risk management. The uncritical assumption that free trade constitutes an unalloyed public good has been undermined by enduring imbalances and the asymmetries of globalization. In this light, calls for a “new Bretton Woods moment” should not entail replicating the rigid institutional blueprints of the past but rather fostering institutional alignment and systemic coherence. The original Bretton Woods architecture thrived not as a monolithic order but as a networked system of institutions, anchored in social-democratic compromise and adaptable governance. Future reforms must draw inspiration from this capacity for institutional evolution, emphasizing the need to restore legitimacy and balance in the multilateral system.

100. Crucially, monetary reform in the present era must go beyond the Keynesian triad of economic efficiency, liberty, and social justice. It must confront the structural incentives that promote global monetary hoarding and asymmetrical adjustment. Today’s challenges are compounded by deeper financialization and its entrenched elite interests that distort both domestic and international policy responses. The persistent accumulation of surpluses in some economies, juxtaposed against austerity-induced stagnation in others, reproduces instability. For example, the U.S. reliance on continuous capital inflows, that are mostly invested in Treasuries and ‘innovative’ debt contracts, into an increasingly fragile financial architecture exposes vulnerabilities that extend beyond traditional macroeconomic indicators. Domestically, rising inequality and a fiscal regime skewed toward *financial capitalism*—rather than households or productive investment—create chronic deflationary pressures and further erode the social contract.

101. Meaningful reform requires rebalancing these asymmetries through shared adjustment mechanisms. The burden of adjustment must not fall solely on deficit economies; surplus countries must also commit to structural changes that stimulate global demand and reduce dependency on external markets. Domestically, financial regimes oriented around consistent, equitable credit access and state-directed financial instruments can mitigate excess liquidity hoarding. Globally, an equitable monetary order necessitates moving away from a single-nation reserve currency toward a multilateral arrangement that supports balance and symmetry in global finance.

102. Equally, the centrality of the state in steering national economic outcomes must be preserved. The success of the original Bretton Woods system was inseparable from its respect for national sovereignty within a cooperative framework. A viable multilateralism for the 21st century must enable state-led development tailored to local conditions, while providing institutional guardrails to manage shared challenges. Importantly, economic multilateralism is not insulated from power politics—it reflects and is shaped by them. Bretton Woods was as much a geopolitical compact among like-minded nations as it was an economic framework. Today’s international order must therefore broaden the definition of “like-mindedness” to accommodate a more diverse and pluralist world. Failure to do so risks reproducing the inequities and exclusions that ultimately eroded the legitimacy of the postwar order.

103. The Trump administration’s imposition of the so-called “Liberation Day” tariffs has brought this need for reform into sharp relief. It marks not merely a rupture in trade policy but an existential challenge to the viability of cooperative economic governance. The IMF’s inability to activate even its limited surveillance functions—let alone galvanize collective action through

forums such as the G20—underscores a systemic vacuum in global macroeconomic coordination. This institutional inertia allowed trade imbalances to widen and competing industrial strategies to clash unchecked.

104. To address this, procedural innovation is both urgent and feasible. The IMF Executive Board, building on its External Sector Report (ESR), could initiate a time-bound Policy Coordination Action Matrix. This matrix would distil actionable, symmetrical policy recommendations for economies with both excessive surpluses and persistent deficits. Crucially, this framework should be elevated to the G20 Finance Ministers and Central Bank Governors as a foundation for consensus-driven deliberations. Embedding such a mechanism within the G20 Leaders’ Summit could shift global economic governance toward a more transparent, accountable, and politically salient arena. By anchoring external sector adjustments within a broader multilateral context, this approach would enhance the legitimacy and efficacy of global economic coordination.

105. In short, the pathway forward demands neither nostalgia for Bretton Woods nor a wholesale rejection of globalization. Rather, it requires an adaptive institutional imagination—one capable of mediating between the imperatives of national sovereignty and the exigencies of policy coordination in a multipolar global economy. Only then can the long-neglected Keynesian vision of a balanced, just, and durable international economic order be realized.



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HOUSE 1, STREET 58, F-7/4, ISLAMABAD, 44000

**TEL: +92 (51) 8 31 43 38**

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