Webb, Michael C., “International Economic Structures, Government Interests, and International Coordination of Macroeconomic Adjustment Policies,” *International Organization* 45 (Summer 1991), pp. 309-342.

Central Question:
What is the impact of international capital market integration on patterns of international coordination of macroeconomic adjustment policies?

Help! I don’t know anything about macroeconomics! (I don’t either.)
What are macroeconomic adjustment policies? The levers by which governments can control the flow of trade and capital across borders, adjust their currency’s exchange rate, finance balance of payments deficits, and monetary and fiscal policy. Why do states want to use these? Because of trade imbalances and interest rate differentials. If goods (or capital) are flowing into (or out of) your country faster than they are flowing out (or in), then that can indicate that your national economy is weaker relative to others.

Central Argument:
The increase in capital mobility that occurred between the 1960’s and 1980’s changed the pattern of national coordination on macroeconomic policy. Specifically, nations stopped managing international payments imbalances by coordinating balance of payments financing, and they started coordinating monetary and fiscal policy instead. When national markets were relatively insulated from transnational linkages by trade and capital controls, payments imbalances (generated by divergent fiscal and monetary policies) could be managed without having to coordinate the fiscal and monetary policies themselves.

Competing Explanations:
Hegemonic stability theory, liberal institutionalists, and neo-Marxists all argue that the most significant change in the international economy over the same time period was the adoption of flexible exchange rates, which increased national macroeconomic policymaking autonomy. This change was seen as a sign of the USA’s declining hegemony and inability to coordinate the Bretton Woods financial system.

Why are these Arguments Flawed?
Realists have given too much attention to the distribution of national power (where the perceived decline of American power explained international financial outcomes). They did not recognize that the structure of the international economy itself had changed and constrained state behavior. The amount of international macroeconomic policy coordination has remained more or less constant over the examined time period. As a result of state decisions to liberalize trade, international capital flows increased. Policy coordination (where countries finance payments imbalances or set fixed exchange rates) could no longer cope with the higher levels of capital mobility, which made it difficult to stabilize exchange rates without also adjusting monetary policy. Subsequently, policy coordination became the coordination of “internal” macroeconomic policy. Countries could change the international system to reduce the influence of international capital (external macroeconomic policy), but such changes would entail high costs.

Assumptions and Definitions:
Assumption: States pursue favorable domestic economic conditions. (low inflation, low unemployment, economic growth)
International coordination: processes involving negotiation and mutual policy adjustment.
Categories of Macroeconomic Policy (goals of which are to eliminate payments imbalances):
External: the manipulation of trade and capital controls to restrict imports and capital outflows. Also includes adjusting exchange rates unilaterally.
Symptom Management: the financing of payments imbalances by using national reserves, international borrowing or intervening in foreign exchange markets.
Internal policies: adjustments in monetary and fiscal policy to eliminate imbalances in savings, investment and consumption that create trade imbalances and interest rate differentials.

Problem: Changing internal macro. policies (fiscal and monetary) will often conflict with the preferences of domestic political groups. As a result, symptom management and external policies entail fewer domestic political costs. However, as international capital became more and more mobile, external and symptom management strategies became less effective or more difficult to manage. Coordinated intervention in the foreign exchange markets cannot stabilize rates when foreign exchange trading has a higher volume than central bank reserves. As a result, governments must adjust their own internal policies, or coordinate with others to adjust theirs.
Coordination entails persuading foreign governments to adjust their internal policies to manage imbalances. Specifically, "deficit countries favor international policy coordination that sees surplus countries reflating their economies, revaluing currencies, expanding their imports, and helping debtor countries finance their deficits" and vice versa. Also, countries will seek to limit other countries from using "external" policies to adjust imbalances. Specifically, "surplus countries [want] to deter deficit countries from restricting imports and sharply devaluing their currencies and to encourage deficit countries to rely on the internal strategy of deflation."

However, structural asymmetries can affect the pattern of coordination, for example, deficit countries with large domestic markets (ie. USA) can improve their bargaining position vis-à-vis surplus countries by threatening to close their markets.