



Title: Global Financial Warriors: The Untold Story of International Finance in the Post-9/11 World

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As the title suggests, *Global Financial Warriors* provides an insider's account of the United States response to a myriad of financial challenges following the 9/11 attacks. The author, John Taylor, under secretary of Treasury for International Affairs (2001-2005), was largely responsible for the creation of teams of "financial warriors" – an international coalition of mostly anonymous experts from state agencies, international financial institutions and private businesses.

Global Financial Warriors can be read and digested on several levels. On one level it is simply a series of stories of these teams carrying out such tasks as staving off financial crises, rebuilding collapsing economies or cutting short the flow of money to terrorist and criminal organizations. Here there are fascinating accounts of dramatic events and complex personalities in dangerous or exotic places like Iraq, Afghanistan, Argentina, or Turkey.

On another level one finds, contrary to the popular perception of a crony dominated, ideologically driven administration, a US government and bureaucracy approaching complex problems with top-notch teams of objective, dedicated and highly competent technocrats. How these teams responded to crises and developed operational procedures to combat them is a story in and of itself.

Finally, on another level, and one appreciated most by professional economists, is Taylor's account of how he took many of his theoretical breakthroughs developed over the years and applied them in solving complex policy problems in crisis situations.

Since the 1970s John Taylor has been instrumental in shaping and extending macroeconomic theory by systematically examining how individuals would anticipate policy changes. His work has been particularly significant in the area of rational expectations. This led to a new emphasis on policy regimes rather than one time changes in policy instruments. Because of his path-breaking work, thinking about future contingency

plans has become a necessary part of macroeconomic policy analysis. This was a major extension of the old Keynesian models into what now is often dubbed “New Keynesian Macroeconomics.”

Just as the original Keynesian theory arose in the 1930s as a response to the incompleteness of the existing classical schools of economic theory, New Keynesian Macroeconomics arose as a response to the criticisms that traditional Keynesians lacked a microeconomic foundation for their theories of the business cycle. Using this framework, Taylor went on to advocate the “Taylor Rule” which posits that adhering to a simple rule or strategy whereby a central bank sets the federal funds rate in response to two variables – inflation and deviations from potential output – is a useful way to conduct monetary policy. He maintains that such a rule could keep inflation low and stable without the “stop-go” fluctuations in output that have plagued many economies in the post-war era. A close reading of Federal Reserve policy actions in the United States have led many researchers to conclude that the Taylor Rule has been the de-facto principle underlying the highly successful period of Alan Greenspan.

Ironically, in many ways, Taylor’s career mirrors that of Keynes. Both were high powered academics specializing in macroeconomic theory. Both rose to top-level administrative positions in their respective national Treasuries. Both were able to draw on years of theoretical work and reflection to guide their policy making. Keynes drew on his theories of finance and aggregate demand to make major contributions to the development of the peace-time, post-war international financial system, while Taylor’s work stressing the superiority of policy rules or principles over discretionary policy making has played a similar, albeit lower profile, role in structuring the United States’ financial response to the problems posed by the rise of terrorism and conflict in the post 9/11 world.

The two differ when it comes to policy goals. Keynes gave legitimacy to short-run discretionary economic policy to attain better rates of employment, whereas Taylor focuses on the attainment of longer-run stability where policy successes are assumed to follow from clear understandable principles. “Principles provide an anchor or a guide, which is especially useful when you can be thrown off track by pressures. The more confidence you have in the principles the better. Taylor notes that he used this principles concept relentlessly while at the Treasury. His staff called them the ten “Taylor Rules,” an extension of the Taylor Rule he had developed for monetary policy years earlier. The rules include:

1. Economic policy should aim to increase economic stability and economic growth.
2. Official finance should support good economic policy with strong ownership. It cannot substitute for bad economic policy.
3. Raising productivity growth is essential for reducing poverty. This requires economic freedom that eliminates impediments to efficient allocation of capital and labor and to the spread of technology.
4. The private sector – not the government – is the engine of economic growth.
5. The international financial system works better when official lending decisions and sovereign debt restructuring processes are predictable. This encourages more efficient movement of capital.
6. Contagion is not automatic. It can be contained by good policy, the dissemination of information and greater predictability in the international financial system.
7. Loans should not be made when there is a high probability that they will be forgiven. Assistance for the poorest countries should be in the form of grants, not loans.

8. Development assistance must produce measurable results. All donors should set clear goals and guidelines. Success should be measured by whether these goals and timelines are met, not by the volume of disbursements.
9. Monetary policy should focus on price stability. Sound exchange rate policies support this objective, prevent crisis, and allow adjustment throughout the global financial system.
10. Tax systems with broad bases, efficient administration, and low marginal tax rates are best to encourage both growth and sustainable public finances.

“The concept of principles applies both broadly and to specific initiatives. We applied No. 1 to everything we did. We applied No. 5 to the IMF reform initiative. We applied No. 6 to the Argentine financial crisis. We applied Nos. 7 and 8 to the World Bank reform initiative.”

Taylor notes that the general principle followed stressed that in a globalized world, finances are a critical part of foreign policy, both as a source of threats and as a policy tool. Financial issues should be treated jointly with the two other pillars of international relations, military and political. “In the case of forming an international coalition to freeze terrorist assets, we stipulated two other overriding principles: that the freeze should be simultaneous and that it should be global. In the case of the reduction of Iraq’s debt, our principle was the greatest possible debt reduction for the Iraqi people and so on.”

However, despite citing numerous policy successes throughout the book, it is apparent that Taylor is a bit defensive – unfavorable comparisons have been made between the Bush Treasury teams of O’Neil/Snow and Taylor and the extremely successful Clinton team of Robert Rubin and Larry Summers. While the book goes a long way to dispel any notion of a fall-off in financial policy making in the Bush Administration, one still wonders how things might have transpired under the more interventionist agenda of Rubin/Summers.

If Taylor’s fascinating accounts have any limitation it is that they are often devoid of this type of critical introspection. As one example, Taylor rightfully takes great pride in providing Iraq with the potential for long-run financial stability with the successful introduction of a new currency; however, the fact is unemployment in that country hovered between 30 and 40 percent during his tenure. In early 2007, the rate of inflation was over 70 percent per annum. Would Rubin/Summers have stressed the more activist short-run policy of a quick disbursement of credit to new business creation as a more direct means of jump-starting that economy, perhaps staving off the economic disaster that has engulfed that country? Alas, we will never know.

Is the world a safer place because of John Taylor, his policy rules, and his teams of dedicated financial warriors? Most certainly it is. Read this book. You will learn how much you do not know. It will change the way you look at the world economy and the United States’ shifting role in attempting to achieve greater stability in the wake of 9/11.