IMF Institutional View:

Time to Deepen Reform

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Three Points

- IV was important but first step for IMF reform on capital account liberalization and management that has continued to evolve but still needs to be deepened
- CFMs have become even more accepted in economics profession and used by EMDs in an environmental that is more volatile
- Three key areas of unfinished business that need to be addressed
  - Make Sure they are in the Toolbox when you need them
  - Focus more attention to advanced economy spillovers and regulation
  - Make sure they are legal!

IMF Articles of Agreement

(Article VI:3)

"Members may exercise such controls as are necessary to regulate international capital movements, but no member may exercise these controls in a manner which will restrict payments for current transactions"

Reasons to Regulate Capital Flows

- Manage the ‘trilemma” (Mundell-Fleming)
- Mobilize domestic finance (Lewis-Prebisch)
- Transition/sequence ‘capital account liberalization’
- *Pigouvian regulations on inflows to stem ‘financial amplification effects’ of surges in short-term inflows (Korinek et al.)*
- Regulate outflows to stem ‘sudden stops’ and balance-of-payments problems

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THE LIBERALIZATION AND MANAGEMENT OF CAPITAL FLOWS: AN INSTITUTIONAL VIEW

November 14, 2012

Capital Account Liberalization

•Capital account liberalization should be done in a sequenced manner

Managing Capital Inflows

•Allow the exchange rate to appreciate, accumulate reserves, tighten fiscal policy, increase capital requirements

•Use **capital flow management measures (CFMs)**

CFMS on Capital Outflows

• CFMs on capital outflows can be considered in crisis or near crisis conditions.

Multi-lateral Aspects of Managing Capital Flows

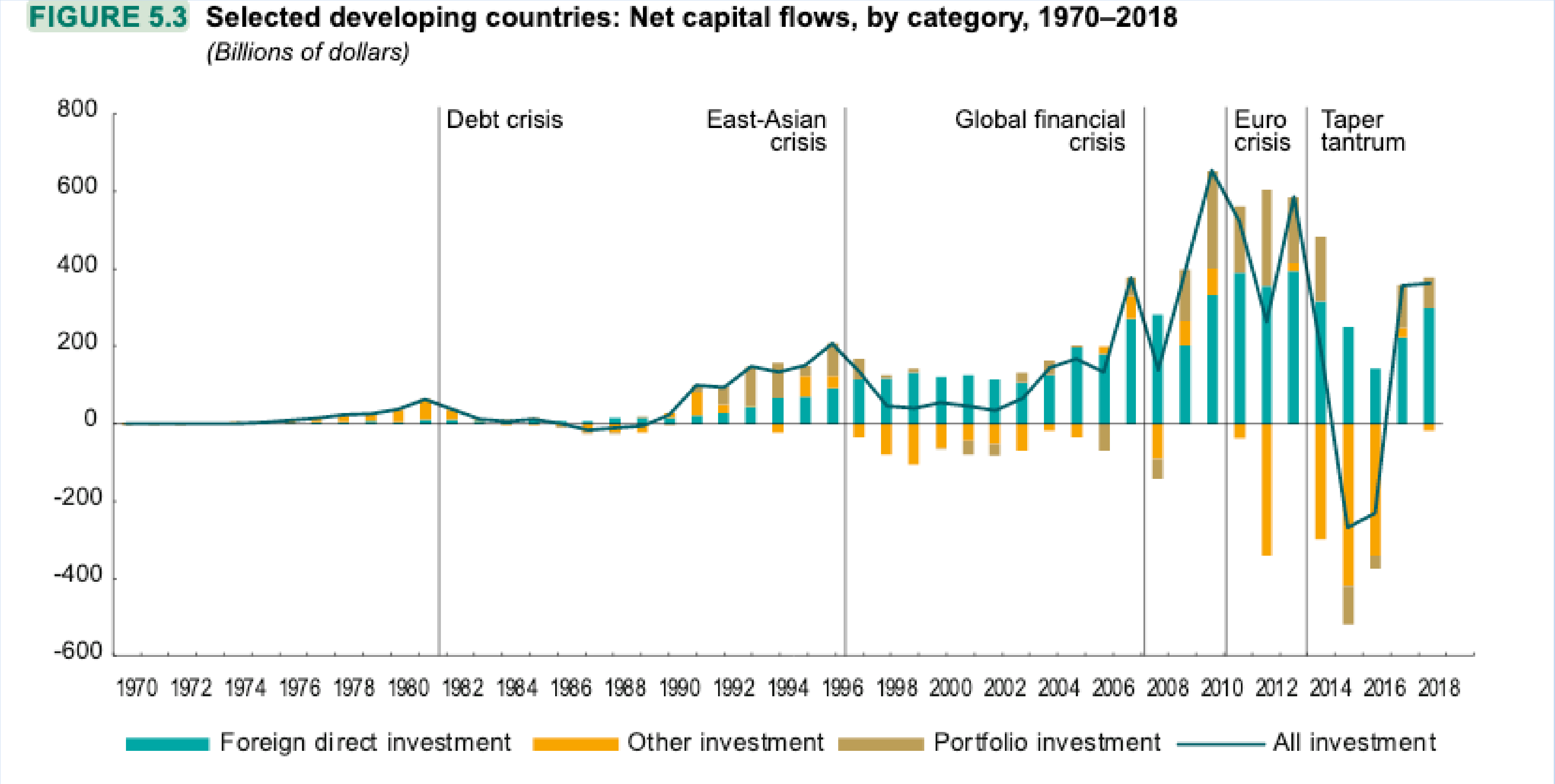
•Nations on both ends of capital flows should be conscious of the multilateral aspects of their policies

•Many trade and investment treaties are at odds with CFMs

1. Seen as measures of last resort and in isolation
2. Biased toward price-based measures
3. Seen as temporary and not permanent part of toolkit
4. Places burden of management on emerging market and developing countries
5. Inconsistent with trade and investment treaties and some IMF programs

https://tinyurl.com/855wm5h0

Surges and Sudden Stops: Capital flows inherently unstable



Source: UNCTAD, Trade and Development Report, 2019

CFMs on the Rise and Effective

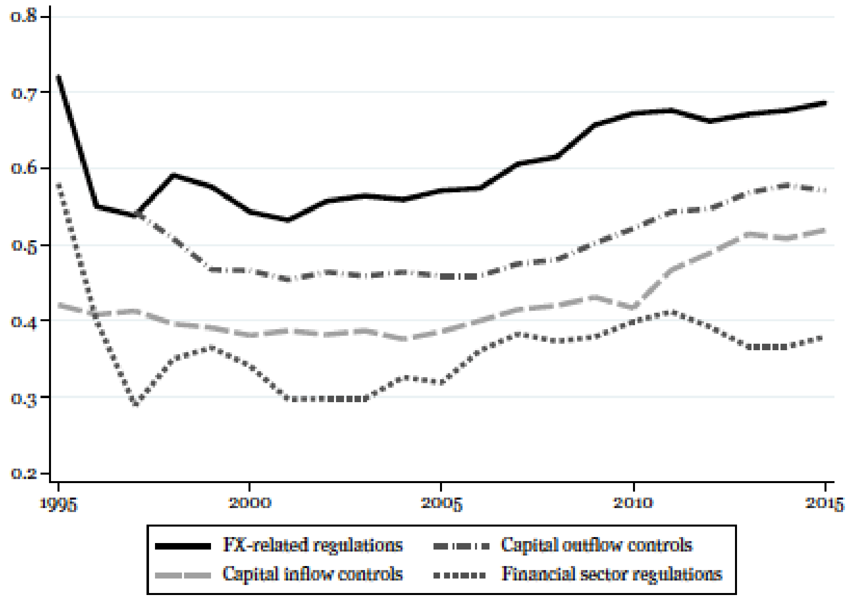


Figure 5: Capital account regulations, 1995 – 2015

Source: Erten and Ocampo (2017) based on data from the IMF's Annual Report on Exchange Arrangements and Exchange Restrictions (AREAER) database

Erten, B. and J.A. Ocampo. 2017. Macroeconomic Eects of Capital Account Regulations. IMF Economic Review 65 (2): 193-240.

Three Generations of EMD Cross-Border Financial Regulations

Country	First Generation (quantitative controls)	Second Generation (price-based controls)	Third Generation (FX regulations)
China	outright bans or limits on the entry of certain investments		
India	Direct limits on USD-ruppe trades		margin requirement on dollar-rupee forward trade increased to 100 percent
Brazil		taxes on portfolio investments	non-interest reserve requirement on bank's short dollar positions in FX spot market
South Korea		witholding tax on non-resident holdings of treasury and monetary bonds	numerous restrictions on bank's FX derivatives positions
Peru		taxes on portfolio investments	position limits on FX short dollar trades and reserve requirements for all FX deposits
Indonesia	one month holding period on central bank bills		
Thailand		taxes on non-resident purchase of public bonds	

Source: Gallagher, 2015, Ruling Capital: Emerging Markets and the Reregulation of Cross-border Finance, Cornel University Press.

IMF: from obstacle to advocate

IMF Advice on Regulating Capital Flows before and after Lehman Crash

Year	*Brazil*	*Chile*	*Colombia*	*Indonesia*	*Mexico*	*Peru*	*South Africa*	*South Korea*
2004			not supportive					
2005								
2006								not supportive
2007			not supportive					not supportive
2008			not supportive					not supportive
2009	Not supportive			Partially		Partially		not supportive
2010	supportive		Partially*	Partially		Partially	supportive	not supportive
2011	supportive		Partially*	Partially	supportive*	Partially	partially*	partially
2012	supportive				supportive*		partially*	partially

*indicates situations where the IMF recommended the use of capital account regulations but they were not deployed by host country in all other cases the IMF is giving some level of support for measures initiated by the host country

Tian, Yuan and Kevin P. Gallagher (2017), "Regulating Capital Flows in Emerging Markets: the IMF and the Global Financial Crisis," Review of Development Finance Volume 7, Issue 2, December 2017, Pages 95-106.

GROUP OF TWENTY

The IMF's Institutional View on Capital Flows in Practice

Prepared by Staff of the

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* The note does not necessarily reflect the views of the IMF Executive Board.

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IMF POLICY PAPER

CAPITAL FLOWS—REVIEW OF EXPERIENCE WITH THE INSTITUTIONAL VIEW

December 2016

IMF staff regularly produces papers proposing new IMF policies, exploring options for reform, or reviewing existing IMF policies and operations. The following documents have been released and are included in this package:

- A **Press Release** summarizing the views of the Executive Board as expressed during its December 5, 2016 consideration of the staff report.
- The **Staff Report**, prepared by IMF staff and completed on November 4, 2016 for the Executive Board's consideration on December 5, 2016.

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

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IMF POLICY PAPER

TOWARD AN INTEGRATED POLICY FRAMEWORK

October 2020

IMF staff regularly produces papers proposing new IMF policies, exploring options for reform, or reviewing existing IMF policies and operations. The following documents have been released and are included in this package:

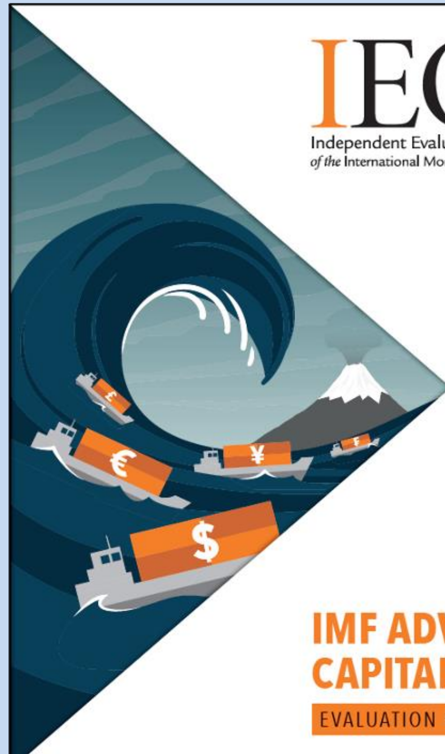
- A **Press Release** summarizing the views of the Executive Board as expressed during its September 28, 2020 consideration of the staff report.
- The **Staff Report**, prepared by IMF staff and completed on September 2, 2020 for the Executive Board's consideration on September 28, 2020.

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

IEO

Independent Evaluation Office

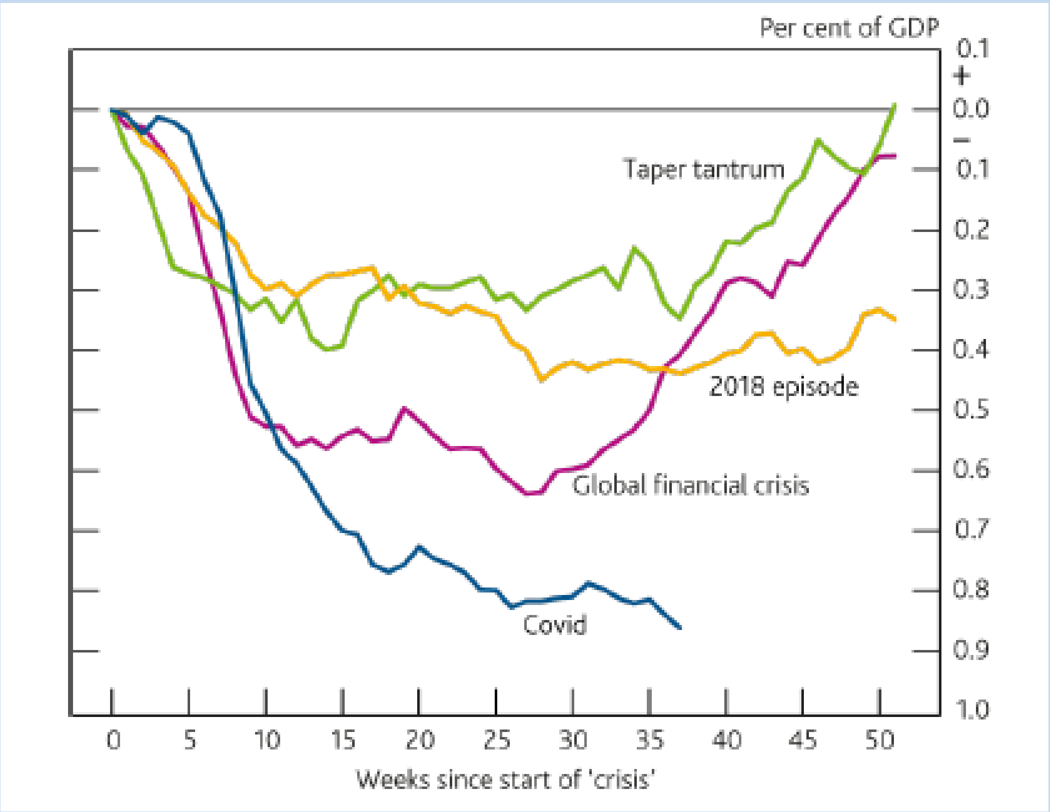
of the International Monetary Fund

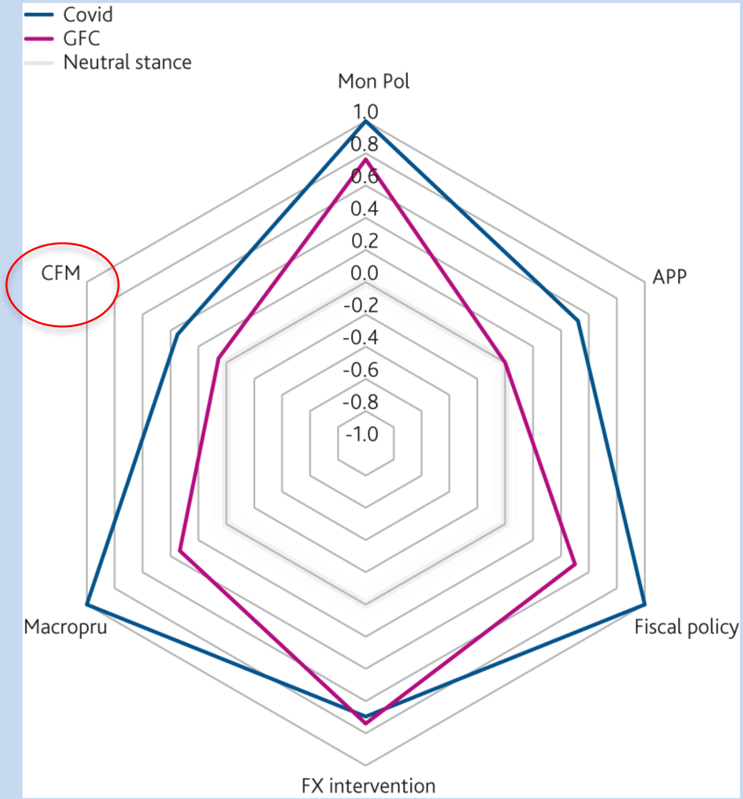


IMF ADVICE ON CAPITAL FLOWS

EVALUATION REPORT 2020

Capital Flows and CFMS in COVID-19 ERA





Bank of England (2020), Capital flows during the pandemic: lessons for a more resilient international financial architecture, December.

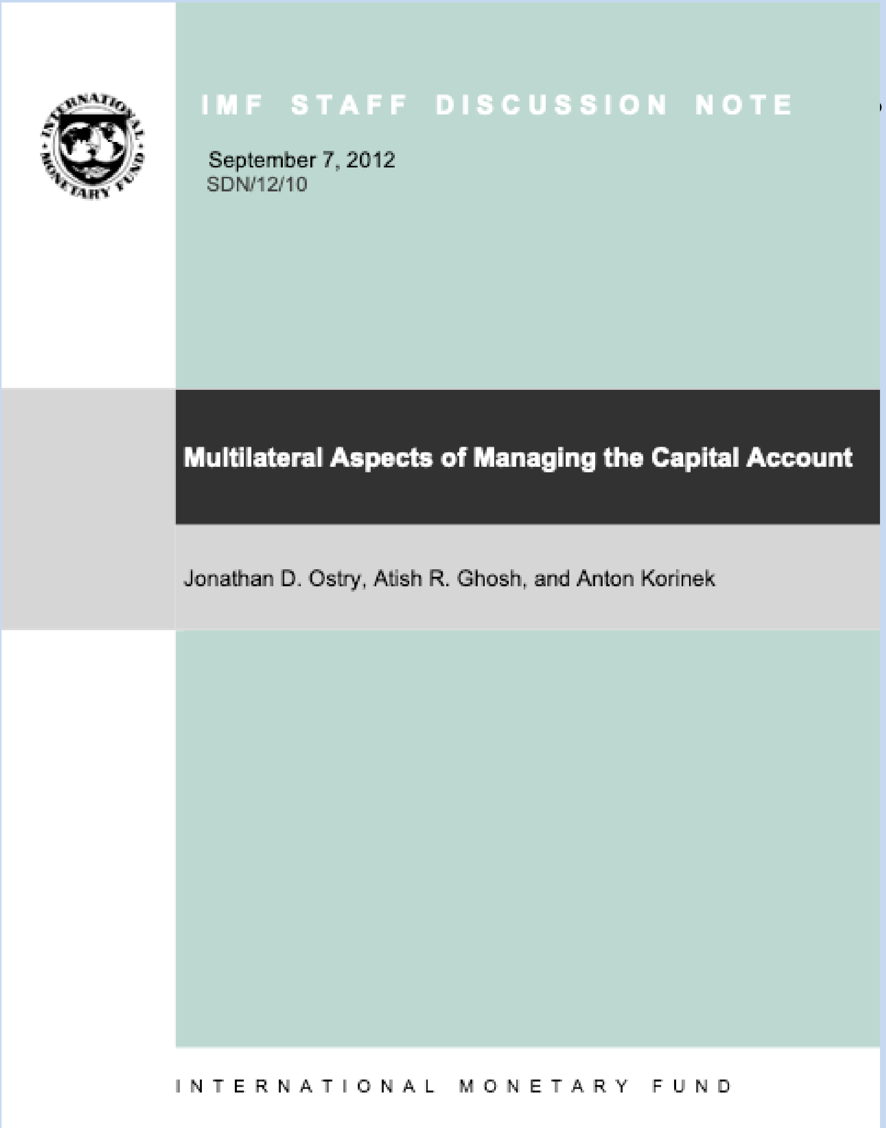
Need to Deepen Reforms

UNFINISHED BUSINESS

1. Make Sure CFMs are in Toolbox

- Countries should have legislation and jurisdiction that permanently allows financial authorities to put in place counter-cyclical regulations on inflows and outflows of capital on a temporary basis as needed.
- CFMs should not be seen as a ‘last resort.’ Evidence shows they work best alongside other macroprudential regulations and FX moves, not after them.

2. Regulate Capital at ‘Both Ends’


IMF STAFF DISCUSSION NOTE

September 7, 2012
SDN/12/10

Multilateral Aspects of Managing the Capital Account

Jonathan D. Ostry, Atish R. Ghosh, and Anton Korinek

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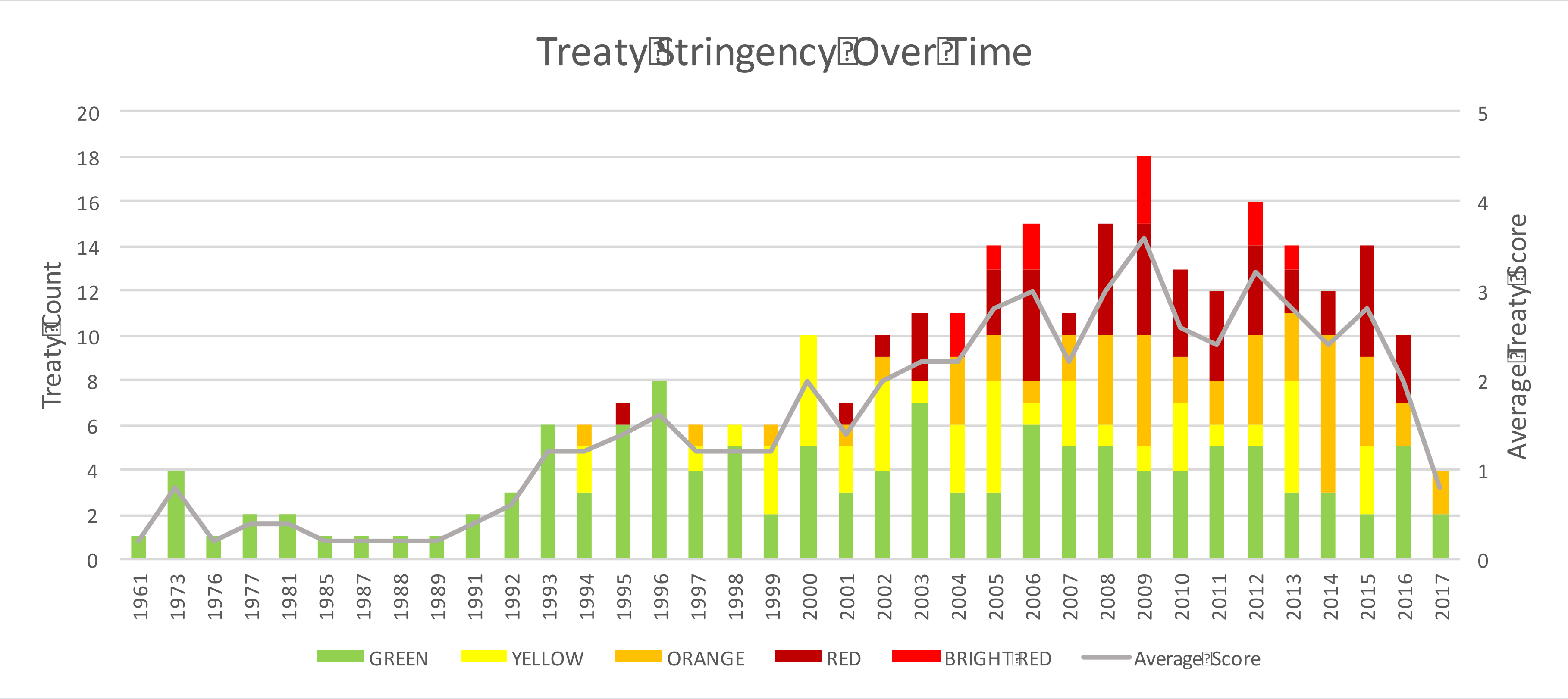
- Coordination involving both source and recipient countries, while very much of the essence, will be more difficult to secure given that source countries may not always find it in their interest to bear (part of) the costs of greater financial stability in recipient countries. The purpose of coordination however is not to enjoin countries to pursue policies that are contrary to the domestic interest; rather, and in consonance with the recently adopted Integrated Surveillance Decision by members of the IMF, it is to choose those policies that meet domestic objectives but have relatively less damaging outward spillovers for the rest of the world.

3. Make Sure they are Legal!

Align national policy with international obligations



Gallagher et al, 2019, Quantifying the Policy Space for Regulating Capital Flows in Trade and Investment Treaties, G-24 Working Paper

IMF on safeguards and Trading System

•**these agreements in many cases do not provide appropriate safeguards or proper sequencing of liberalization**, and could thus benefit from reform to include these protections (IMF 2012a, 8)."

•"In particular, the proposed institutional view could help foster a more consistent approach to the design of policy space for CFMs under bilateral and regional agreements. Recognizing the macroeconomic, IMS, and global stability goals that underpin the institutional view**, members drafting such agreements in the future, as well as the various international bodies that promote these agreements, could take into account this view in designing the circumstances under which both inflows and outflows CFMs may be imposed within the scope of their agreements (IMF 2012b, 33).**

International Monetary Fund (2012a), Liberalizing Capital Flows and Managing Outflows, Washington, IMF.

International Monetary Fund (2012b), The Liberalization and Management of Capital Flows: An Institutional View, Washington, IMF.

Trade Policy Reforms

Article 32.4: Temporary Safeguards Measures

1. For the purposes of this Article:

foreign direct investment means a type of investment by an investor of a Party in the territory of another Party, through which the investor exercises ownership or control over, or a significant degree of influence on the management of, an enterprise or other direct investment, and tends to be undertaken in order to establish a lasting relationship; for example, ownership of at least 10 percent of the voting power of an enterprise over a period of at least 12 months generally would be considered a foreign direct investment.

2. This Agreement does not prevent a Party from adopting or maintaining a restrictive measure with regard to payments or transfers for current account transactions in the event of serious balance of payments and external financial difficulties or threats thereof.

3. This Agreement does not prevent a Party from adopting or maintaining a restrictive measure with regard to payments or transfers relating to the movements of capital:

(a) in the event of serious balance of payments and external financial difficulties or threats thereof; or

(b) if, in exceptional circumstances, payments or transfers relating to capital movements cause or threaten to cause serious difficulties for macroeconomic management.

Source: USMCA

ANNEX 9-E[40]

TRANSFERS

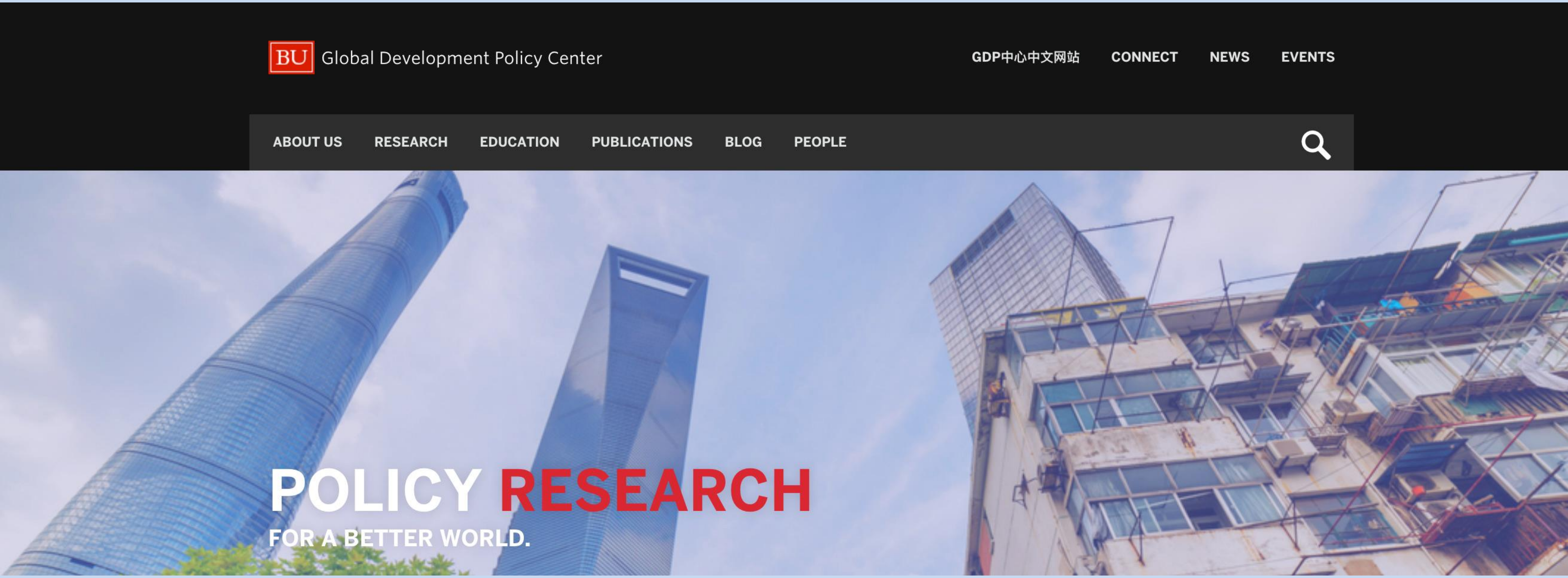
Chile

1. Notwithstanding Article 9.9 (Transfers), Chile reserves the right of the Central Bank of Chile (*Banco Central de Chile*) to maintain or adopt measures in conformity with Law 18.840, Constitutional Organic Law of the Central Bank of Chile (*Ley 18.840, Ley Orgánica Constitucional del Banco Central de Chile*), and *Decreto con Fuerza de Ley Nº3 de 1997, Ley General de Bancos* (General Banking Act) and *Ley 18.045, Ley de Mercado de Valores* (Securities Market Law), in order to ensure currency stability and the normal operation of domestic and foreign payments. Such measures include, *inter alia*, the establishment of restrictions or limitations on current payments and transfers (capital movements) to or from Chile, as well as transactions related to them, such as requiring that deposits, investments or credits from or to a foreign country, be subject to a reserve requirement (*encaje*).

2. Notwithstanding paragraph 1, the reserve requirements that the Central Bank of Chile can apply pursuant to Article 49 No. 2 of Law 18.840, shall not exceed 30 per cent of the amount transferred and shall not be imposed for a period which exceeds two years.

Trans-Pacific Partnership Agreement

THANK YOU!



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