Global governance of capital flows: the view from the IMF

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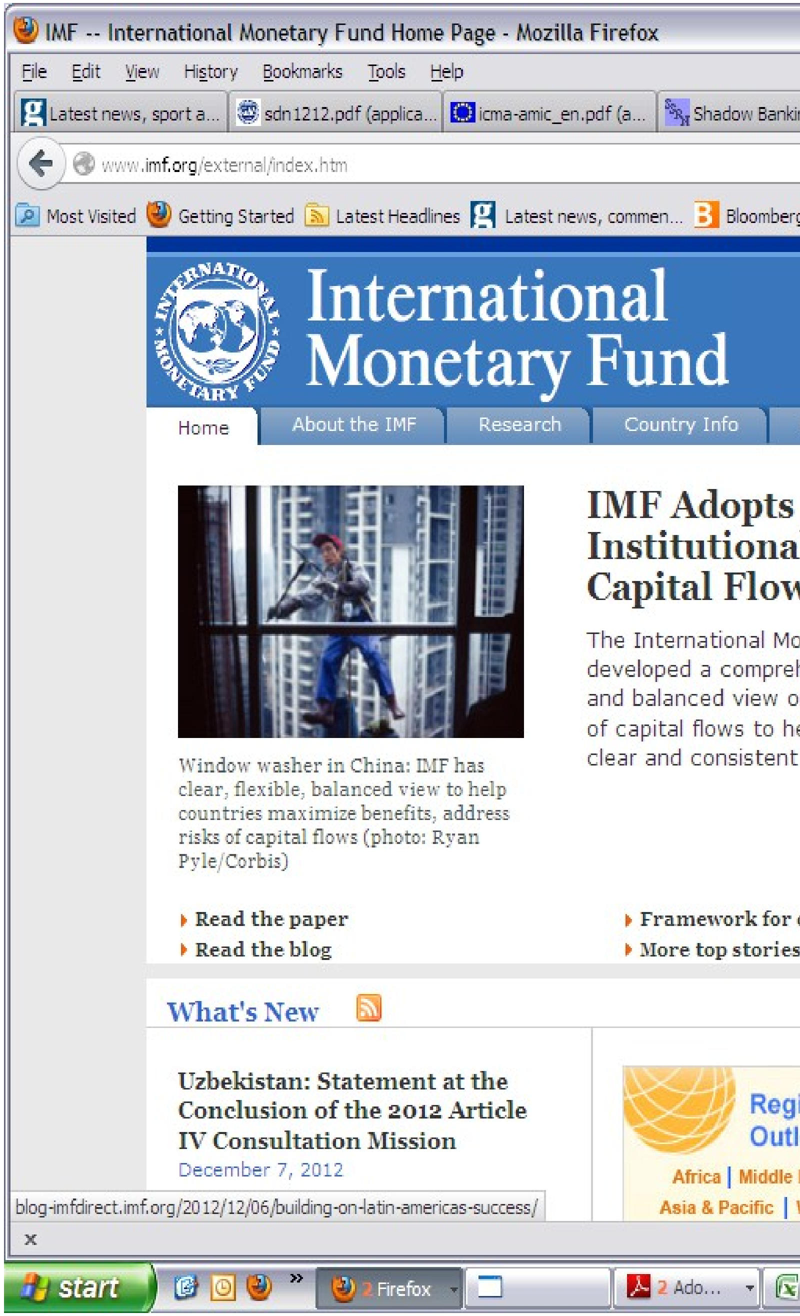
“non-resident investors behave in a systematically different way to residents”
Brazil’s representative at the IMF, Financial Times, Dec. 5



In this presentation

- A critique: the IMF's change is cosmetic
  - The institutional view pays no analytical attention to financial institutions that intermediate capital flows (at least until WEO 2013; Gabor, 2012)

- We should think *interconnectedness*:
  - global financial architectures, global banks and fragile connections these sustain within and across borders (Haldane, 2009; IMF, 2010; 2012; Bruno and Shin, 2012; Brunnermeier et al. 2012; Gabor, 2013)

The view from the IMF's window

- Macropolicy first, then capital controls
- Control inflows rather than outflows
- Treat domestic and foreign investors equally

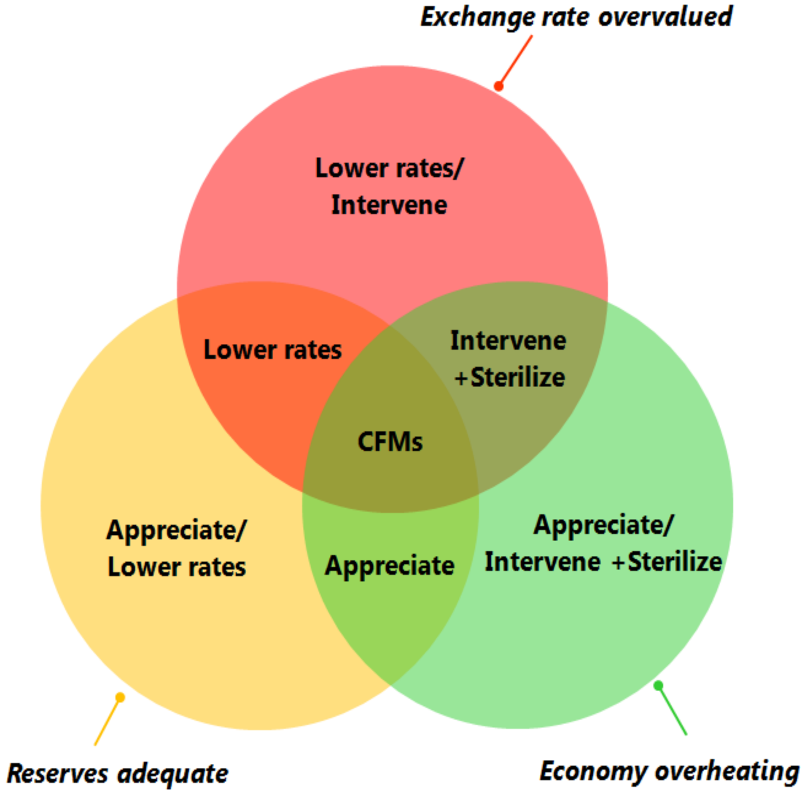
The preference for non-discriminatory measures mainly reflects a regard for the general standard of fairness and equal treatment that Fund members expect their nationals will enjoy as a result of members' participation in a multilateral framework like the Fund.

IMF, 2012: 20

- Domestic investors – stabilizing financial adjustment (WEO 2013)

The IMF’s ‘code of conduct’ macropolicy first

Figure 3. Managing Capital Inflow Surges

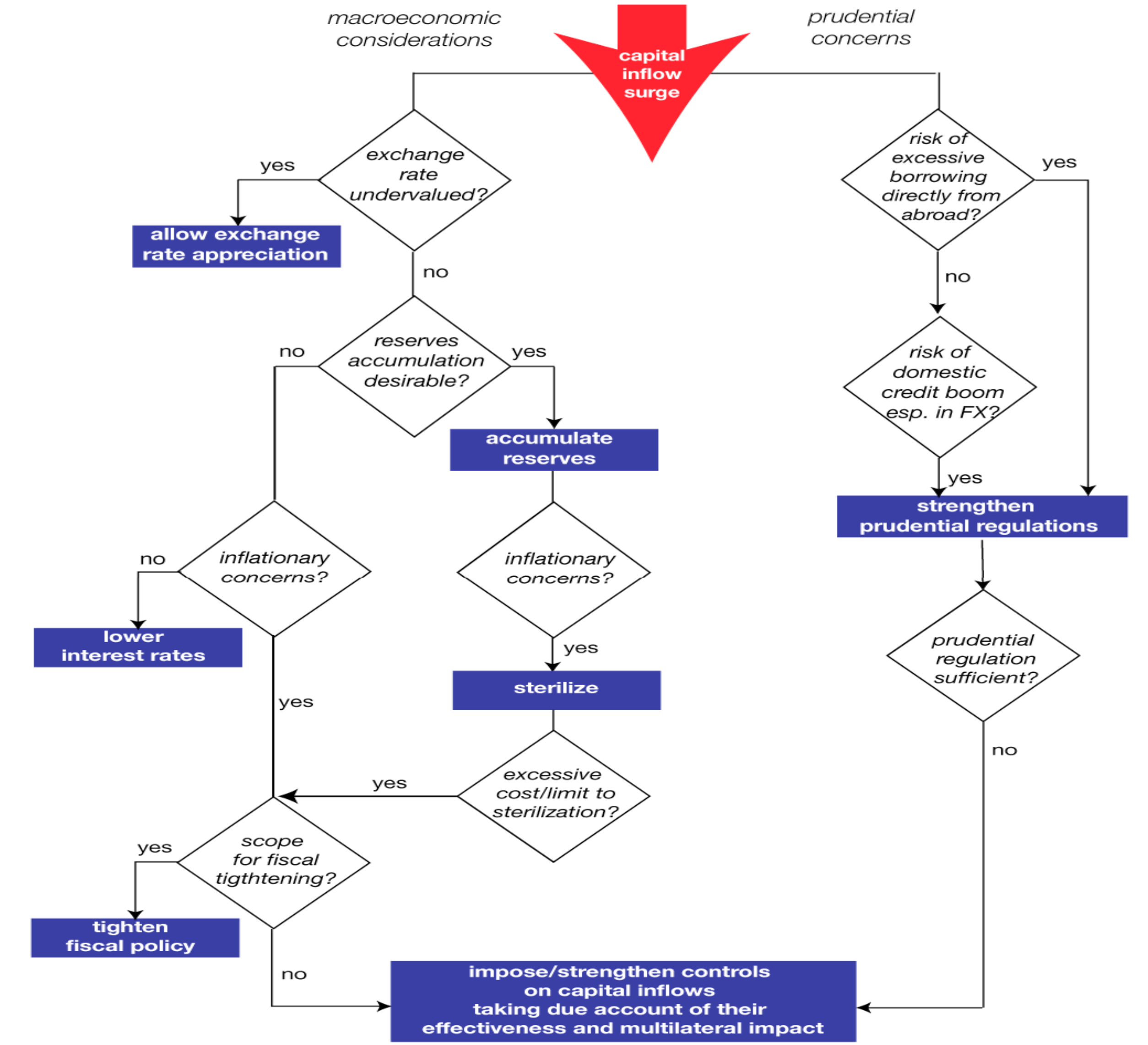


Each circle represents cases where the relevant condition is met. For example, the top circle ("Exchange rate overvalued") represents cases where the exchange rate is assessed to be overvalued. The intersection of all three circles reflects cases where the exchange rate is overvalued, reserves are judged to be adequate, and the economy is overheating.

In such cases of limited policy flexibility, as represented by the intersection of all three circles, CFMs can be useful to support, and not substitute for, the needed macroeconomic adjustment.

CFMs could also be useful **to safeguard systemic financial stability** under certain circumstances. At other times, CFMs can help gain time when taking the needed policy steps requires time, when the macroeconomic adjustments require time to take effect, or when there is heightened uncertainty about the underlying economic stance due to the surge.

Figure 1. Coping with Surges in Capital Inflows: Macroeconomic and Prudential Considerations 1/

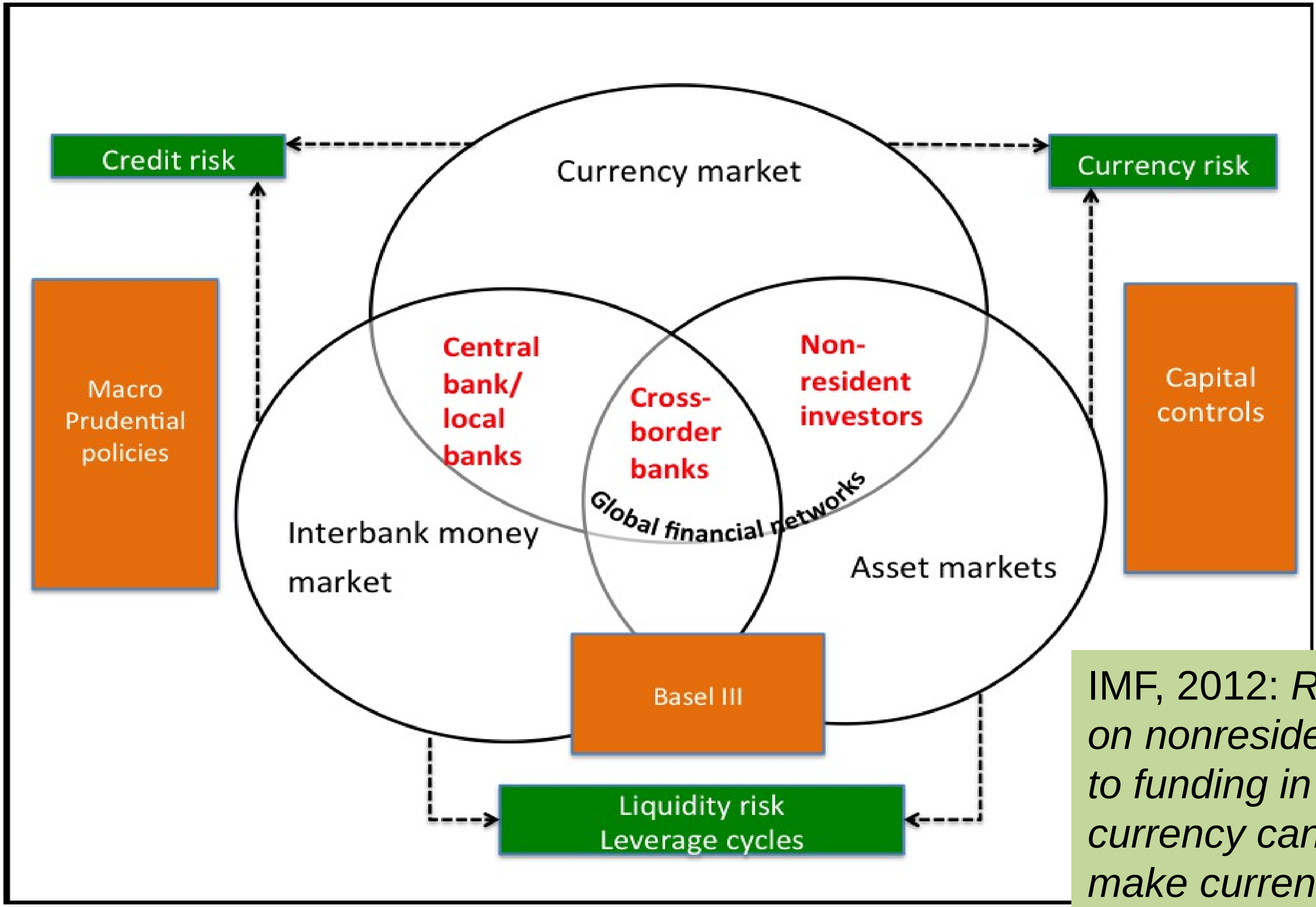


1/ From the perspective of an individual country, without taking account of multilateral considerations; on the effectiveness of controls, see Section III.

The IMF’s macro policy first

- Step 1: Measure misalignment with equilibrium ER theories (but carry-trades?)
- Step 2: Lower interest rates (conservative bias of central banks)
- Step 3: Currency market interventions to accumulate ‘precautionary’ reserves
  - How to measure ‘precautionary’?
- Step 4: Sterilize ‘at all costs’?
  - Steps 3 and 4 particularly problematic from a CFM perspective

Steps 3&4 and cross-border financial architectures



IMF, 2012: *Restrictions on nonresidents' access to funding in local currency can at times make currency speculation more difficult*

So what should the IMF be really looking at?

- Identify vulnerabilities associated with distinctive international financial actors; fragile connections these forge
- The capital controls relevant for each type
- Capital account management requires new models of central banking and private banking