

FSN : How Can Regional and Multilateral Coexist

Raden Pardede

Former Chairman of Indonesian Financial Stability Forum

New Delhi, 17 September 2010



www.crecoconsulting.com

FSN



- ✓ Crisis experience over the last 15 years clearly shows that Modern international finance is volatile and crisis prone
- ✓ It is crucial to have quick access to large amount of cash in order to stave off crisis (in the case of Global FSN : to discourage emerging market nations from hoarding foreign reserves)
- ✓ Five elements of FSN :
 - ✓ Regulation and Supervision
 - ✓ Lender of Last Resort
 - ✓ Bank / FI insolvent Resolution law
 - ✓ Deposit Insurance Scheme
 - ✓ Institutionalized decision making : Cooperation resolution schemes

Regional Stabilization

Mechanism (fund) or (FSN)

- ✓ Available Mechanism (fund/FSN)
 - ✓ European financial Assistance Mechanism
 - ✓ Arab Monetary Fund
 - ✓ Chiang Mai Initiative Multi-lateralization CMI – CMIM (ASEAN +3)
 - ✓ North American Framework Agreement, NAFA
 - ✓ FLAR
- ✓ Element of fund / FSN
 - ✓ Power /Size of fund
 - ✓ Surveillance and monitoring
 - ✓ Speed of decision making
 - ✓ Certainty : voting formula and CMP
 - ✓ Linkage with IMF

Regional Stabilization Mechanism

	Financing Adequacy	Surveillance capacity	Speed	Legitimacy	Ability to work with IMF
EFAM	Big	ECOFIN	Fast	Yes	Co financing
CMI/M *)	120 B with potential increase	AMRO but not yet function	Never been utilized	Yes, with decision making process	Yes, but politically sensitive
NAFA	3 BSA : 9 B	3 MOF	Fast, only BSA	Regular ad hoc consultation	No formal link
AMF	3 B	AMF division	Limited	Yes	No provision
FLAR	2 B paid up capital w ability to borrow	Economic study division	fast	yes	No Formal link

*) Fundamental issue : Review of size, contributions, borrowing multiplier, terms of lending, etc => decided by consensus of ASEAN+3, meanwhile, lending, renewal, default => by majority vote

IMF



- ✓ Schemes/Facilities:
 - ✓ Contingent Credit Line, CCL
 - ✓ Short Term Liquidity facility, SLF/RAL
 - ✓ Flexible Credit Line, FCL
 - ✓ Precautionary Credit Line, PCL
- ✓ (Un) Success story
 - ✓ Asian Crisis : Stigma
 - ✓ Eastern Europe Crisis
 - ✓ Euro (Greek) Crisis, Initially reluctance to ask IMF help but end up with co financing with Euro
 - ✓ FCL reassure the markets: Mexico, Poland, Columbia (credit line of 40B, 20B, 3.4B) even without withdrawn

Asian experience

- ✓ CMI === > CMIM = Has not operated
- ✓ Asian crisis 1997/1998 (Current account and short term cap flows crisis)
 - ✓ Thailand, Indonesia, Malaysia, Korea, ..
 - ✓ Thai, Indonesia and Korea enter IMF program
- ✓ Global crisis 2008
 - ✓ Indonesia, Korea, Singapore
 - ✓ Despite Flexible credit line (FCL) introduced in March 2009, it is political suicide if Korea has to go to another IMF program
 - ✓ Korea and Singapore entered swap agreement with Fed
 - ✓ Indonesia applied BSA but rejected by Fed, but end up BSA with Japan and China
 - ✓ Indonesia establish Contingency Budget financing (Deferred Drawdown Facility- DDF) 5.5B from WB,ADB, Japan and Australia
- ✓ CMI (too small with condition) vs BSA (Fed Discriminatory) vs IMF (stigma issue)
- ✓ BOP (short term debt) vs Budget Refinancing
- ✓ The role of Multilateral Development Bank, MDB (WB and ADB)₆ on DDF Indonesia

CMIM mechanism needs refinement


- ✓ Ability to support fast and effective decision making :
 - ✓ Surveillance : more open and transparent
 - ✓ Avoid the reluctance to discuss weak policies of regional neighbors (avoid ASEAN way)
 - ✓ Implementing and monitoring mechanism
 - ✓ Making AMRO well staffing and well funded
- ✓ Increase power and size
 - ✓ Fund can be supplemented from countries in the group (similar to IMF ++ in 97/98 crisis)
 - ✓ Swap facility with CMIM (faster and flexible)
- ✓ Refine contribution subject to “fiscal, monetary, regulatory” risk profile (similar to CAR for banks)
- ✓ More flexible and no/less conditionality with IMF
- ✓ Fund could be possible to other countries (euro help eastern euro)

Why Coexist beneficial

- ✓ International harmonization and coordination to prevent crisis (systemic and cross-border crisis)
- ✓ Political reason: Regional and Multilateral development banks face less stigma than IMF
- ✓ Complementarities in Surveillance and Decision making
 - ✓ IMF : Global surveillance with strong skill
 - ✓ Regional : more deep and detail info and surveillance. Regional can tap skill from IMF
 - ✓ Regional surveillance should supplement the IMF surveillance
 - ✓ Let regional handle political sensitive decision making ?
- ✓ Bigger Fund (Size/Power) additional supplement fund from IMF but with more effective response to systemic financial crisis
- ✓ Reduce cost of self insurance, i.e. accumulation of low yields reserve asset, especially in Asia

What can we do for further

- ✓ Improve the regional FSN mechanism and make it work more effective operatinally
- ✓ Improve harmonization of regulation across country within the region :
 - ✓ Prevent regulatory arbitrage
 - ✓ Avoid gap in insurance coverage across border (especially at the peak of crisis)
 - ✓ Standardized liquidation of international financial institution
- ✓ Utilize MDB (to be a partner) :
 - ✓ Long run sustainability interest (vs. IMF short run focus)
 - ✓ Financing (counter cyclical) with project and policy based
 - ✓ Support the overall public expenditure framework (fiscal adjustment), help design social protection programs
 - ✓ Pursue growth enhancing reforms

- 
- ✓ **Extend liquidity provision to adjustment and debt restructuring resolution (regional FSN could supplement IMF)**
 - ✓ **Diagnose : solvency vs liquidity**
 - ✓ **Action : continue lending (good equilibrium) vs. Stop lending and panic withdraw (bad equilibrium)**
 - ✓ **Sovereign Debt Restructuring Mechanism**
 - ✓ **Orderly default and hair cut**
 - ✓ **International legal reform (harmonization)**
 - ✓ **Caveat : all facilities should not create moral hazard**
 - ✓ **Clear responsibility of each FSN national, regional, multilateral, and well define linkage among them**

FSN Linkage

National	Regional	Multilateral IMF + MDB
<ul style="list-style-type: none">• Regulation and supervision• LOLR• Resolution and insolvent law• Insurance deposit• Institutionalized decision making : Cooperation resolution scheme (CMP across department)	<ul style="list-style-type: none">• Harmonize : prudential conditionality• Yes• Harmonize : Adjustment conditionality• Harmonize• Regional linkage	<ul style="list-style-type: none">• Harmonize• Yes (Co Financing)• Harmonize• Harmonize• Global linkage