Discussion at G-20 Conference
Capital Controls, Liquidity Provision, and Foreign Investors

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Outlines that there are significant links between countries, raising the likelihood of "innocent bystander" problems and increasing the severity of systemic crises.

Suggests that precautionary credit lines can be beneficial to economies, and help prevent spillover effects.

Explains that a Global Financial Safety Net may be the most efficient way to accomplish this, rather than individual credit lines.

- Relies on connectedness in GDP across countries, a very reasonable assumption.

Q: Should we think about unanticipated consequences/equilibrium effects? (Discussion below).
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- Allowing the IMF to borrow from capital markets.
- Creating a global network of swap arrangements.
- Formalising links between the IMF and RFAs; making it clear ex-ante what scale of resources might be available.

Q1: Even for Eurobond issuance, it comes down to a fiscal policy question. The lesson seems to be that you can’t raise capital unless you have the ability to create fiscal policy/raise taxes as well.
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Q2: Is strategic ambiguity useful when thinking about disclosure on the scale of resources available?
Consider whether capital control tightening in India during the crisis was effective in controlling capital flows.

Present several useful examples that it did not.

One example: maximum permitted interest rate for foreign borrowing dropped by 50-100 bp.

- Attempt to control capital inflows.
- But capital inflows from all other sources increased to compensate.

Q: Doesn’t this raise a broader issue about re-optimization by financial agents in response to policy changes?
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View: New institutions generate (both positive and negative) unintended consequences.
Lessons from Asset Fire Sales
Global funds cut positions in emerging markets in response to domicile-induced funding shocks
Lessons from Asset Fire Sales
Large price impacts especially during crisis periods
Lessons from Asset Fire Sales
Funds reallocate to more liquid markets

<table>
<thead>
<tr>
<th>Decile</th>
<th>Flow (%)</th>
<th>Countries Expanded</th>
<th>Countries Reduced or Eliminated</th>
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<tr>
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<td>10 (Outflows)</td>
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<tr>
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<td>(-3.28)</td>
<td>(6.56)</td>
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- Liquidity provision could thus also have beneficial asset pricing impacts, since trade links generate stock return correlations.
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- Also important to build enhanced levels of reporting and disclosure, in addition to liquidity provision facilities.