

Regional Financial Cooperation to Enhance Financial Resilience and Stability

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 - ❖ Capital flow during financial crises
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Introduction

- ▶ Various issues surrounding RFA in East Asia
 - ❖ Examination of current RFAs in East Asia: e.g., CMIM, ABMI
 - ❖ Link with a broader regional integration: e.g., AEC, regional FTA
 - ❖ RFA-IFI cooperation: e.g., IMF, ADB
 - ❖ Response to external shocks: e.g., US monetary policy

- ▶ The Conference
 - ❖ Promote regional financial cooperation
 - ❖ Improve the function of RFAs in East Asia

Introduction

- ▶ My presentation: focus on the Korean experience
 - ❖ Hit by both the Asian crisis and the GFC
 - ❖ A typical example of regional countries' problems: economic fundamentals vs. financial fragility
 - ❖ A good source to derive some effective and meaningful policy suggestions for financial resilience and stability

Korean Experience

➤ Two cases

❖ Capital flows during financial crises

- Show what is the most important cause of financial crises in East Asia

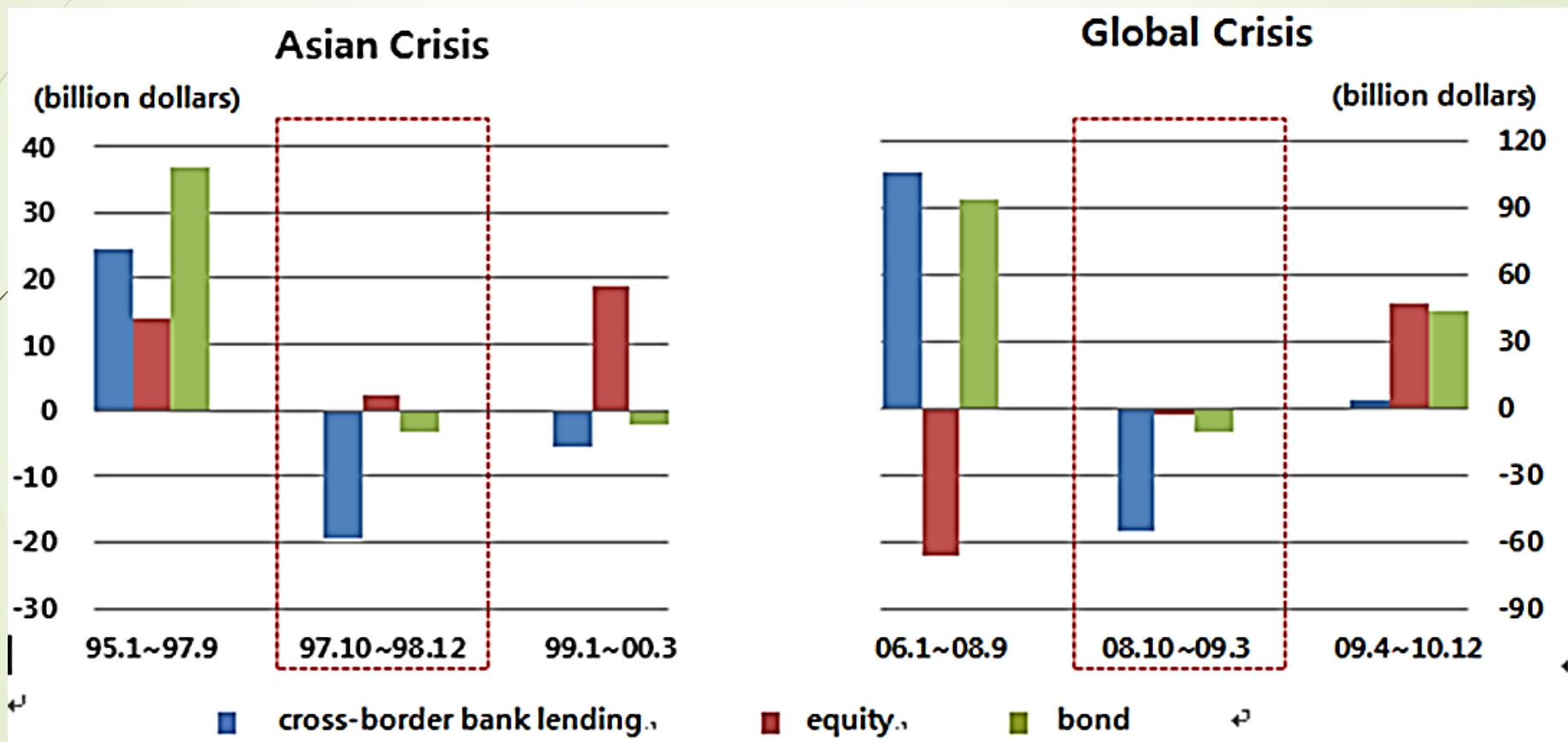
❖ Role of existing financial programs

- Show problems of financial support programs by the IMF and current RFA

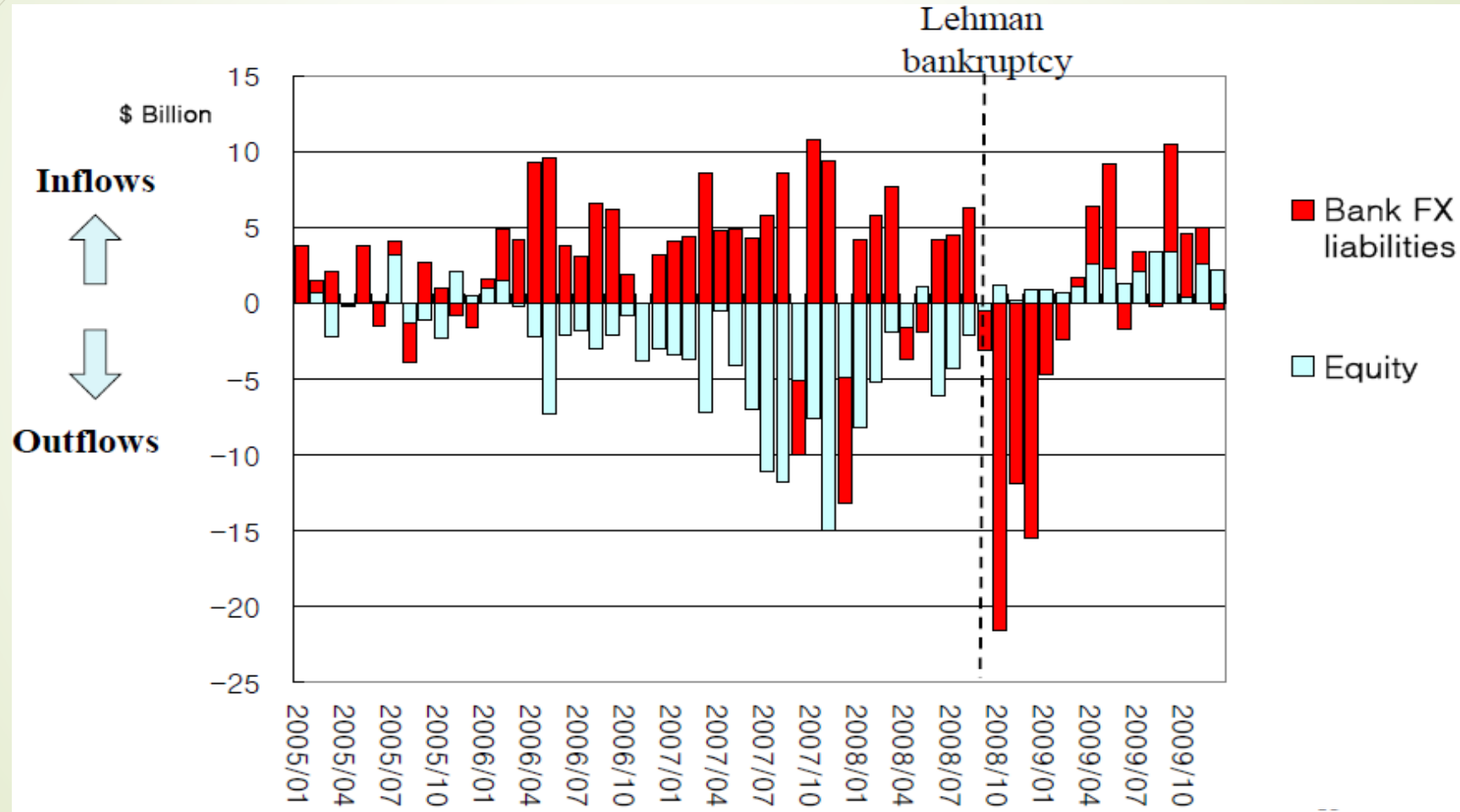
Korean Experience

- Capital flows during financial crises
 - ❖ Underlying causes of financial crises are both external and internal: but more external in East Asia due to volatile international capital
 - Asian crisis: Sudden reversal of private capital flow (in particular, bank borrowings)
 - Global financial crisis: Another sudden reversal of capital from inflow to outflow only within a short time right after the Lehman-Brothers collapse (again, bank borrowings)
 - ❖ Even though the Asian economies were in good shape, it was impossible for them to cope with that huge flow of foreign capital

Capital flows during financial crises



Capital flow during GFC



Korean Experience

➤ Role of existing financial programs

❖ IMF's financial assistance

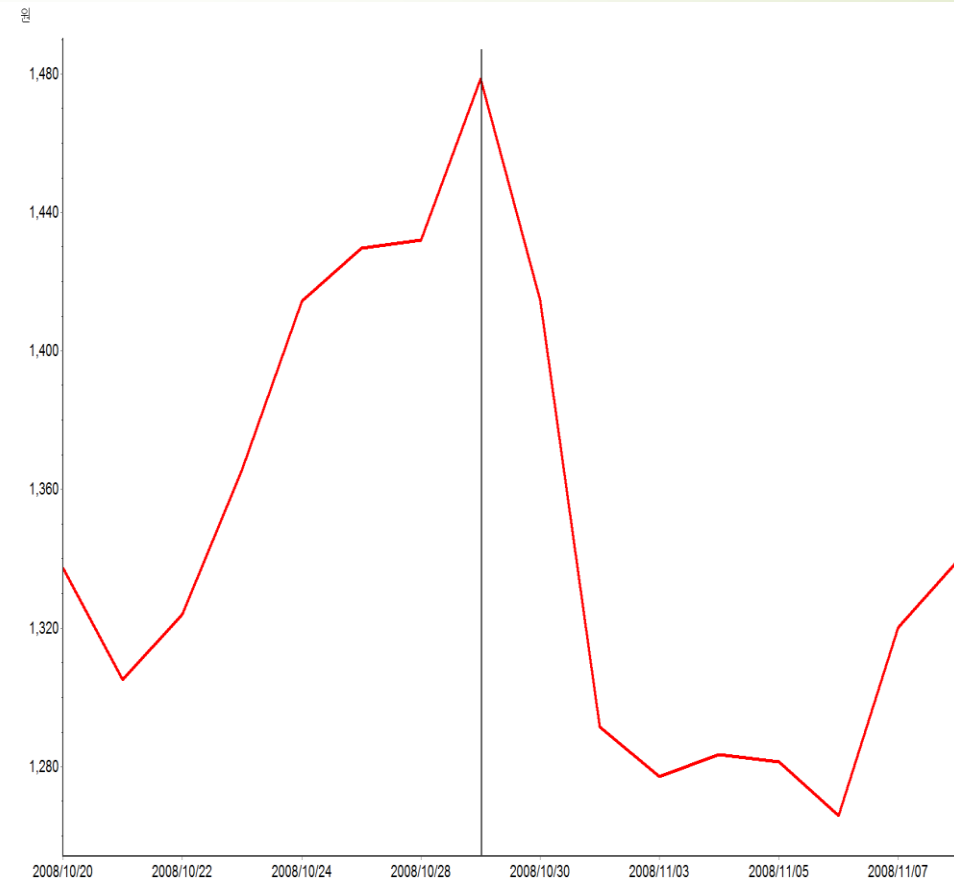
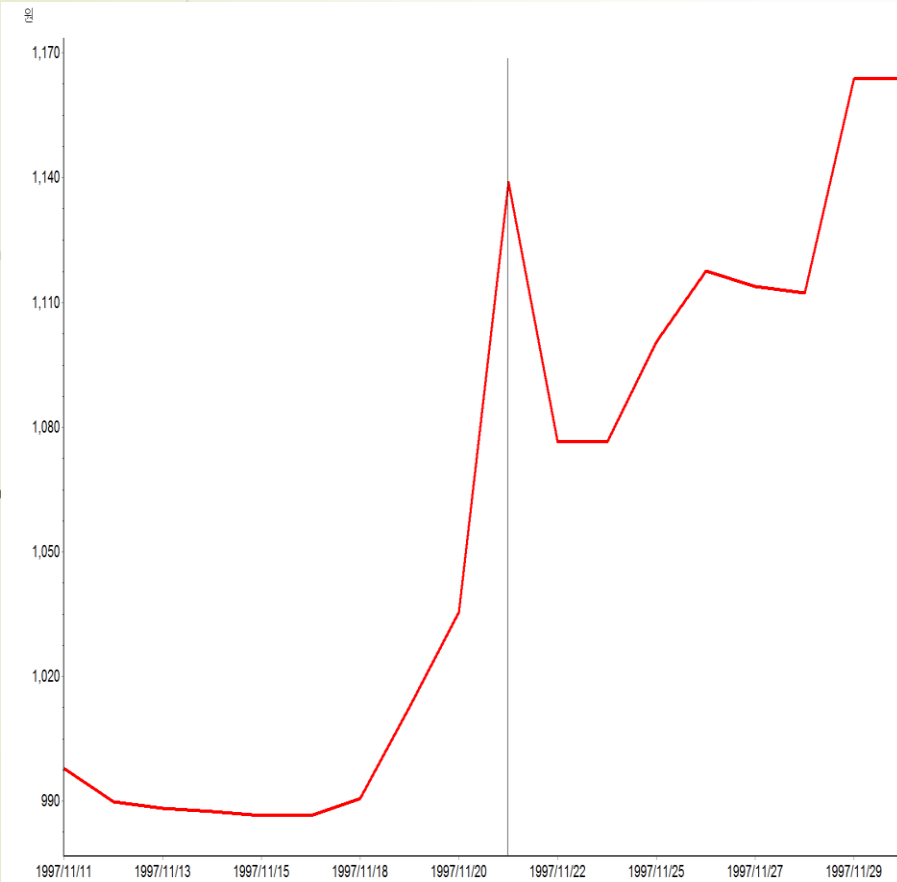
- IMF assistance was not effective in stabilizing the market but only adds severity: Extension of debt maturity helped
- During GFC, did not use IMF's financial credit line due to stigma effect and trauma effect: bilateral swap helped

❖ RFA: CMIM

- Not activated even in times of crisis
- Many problems: size, resource, conditionality, governance

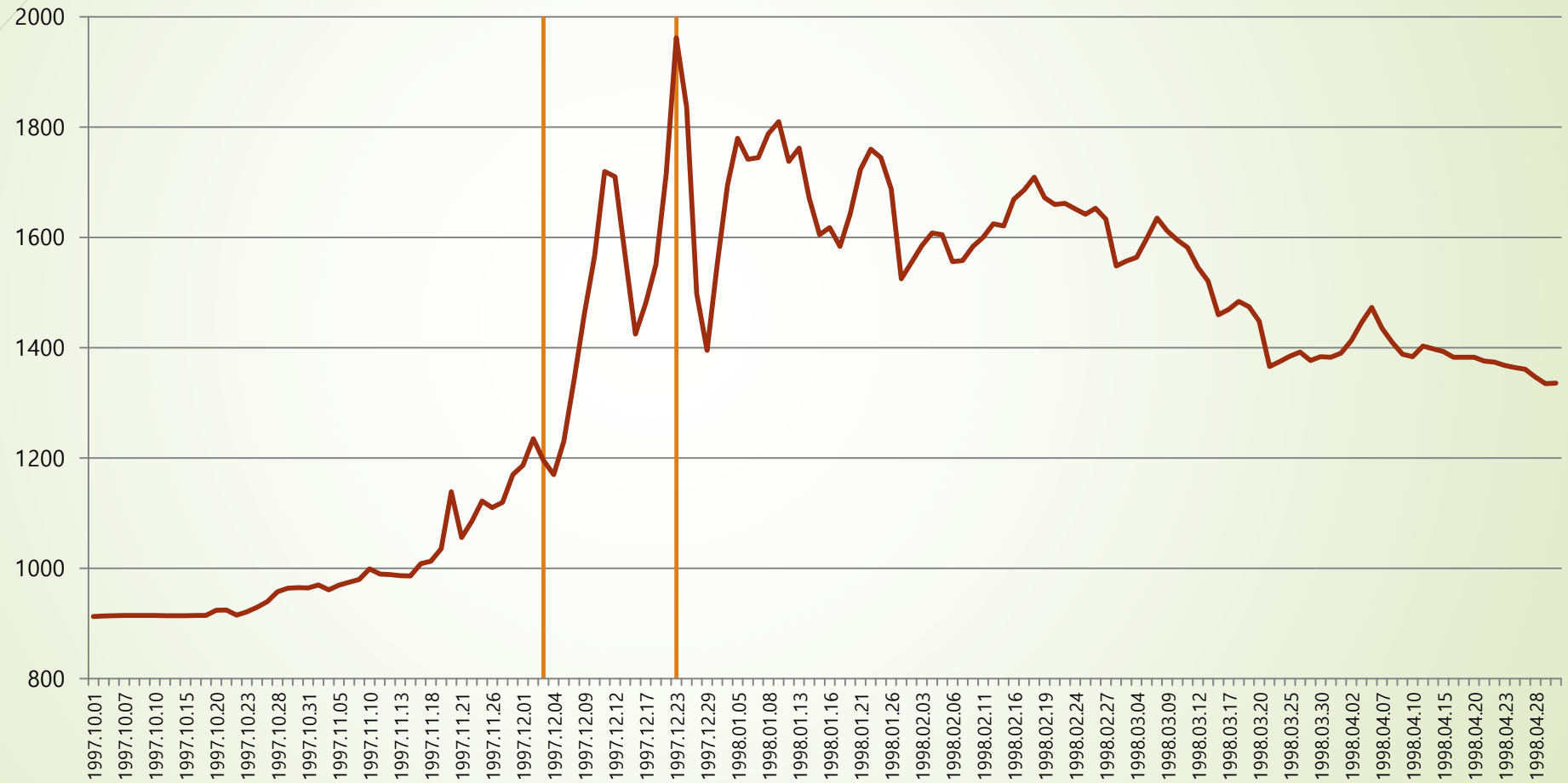
Exchange Rate Movement

1997 vs. 2008



Exchange rate movement

Oct.1997 - Apr.1998



Suggestions

► Monitoring

❖ AMRO

- Monitor, assess, and prepare quarterly reports on macroeconomic situation and financial soundness
- Assess macroeconomic and financial vulnerabilities and provide assistance in timely formulation of policy recommendations

❖ Monitoring of capital flow is the key

- In particular, flow of bank borrowings
- Policy to reduce volatility of capital flow: bank levy

Suggestions

► Provision of international liquidity

❖ IMF, RFA

- Trauma effect, stigma effect
- RFA: only commitment

❖ Permanent currency swap agreement

- Worked during in times of crisis
- Signal of ensuring international liquidity

Suggestions

➤ Others

❖ RFAs in East Asia

- Size, resource, conditionality, governance

❖ RFA-IMF cooperation

- Dismantle the formal link of CMIM financing to the IMF-supported program (Kawai 2009)

❖ RFA-ADB relation

- Division of labor: ADB (development), AIIB (infra-investment), CMIM (financial stability)

Suggestions

➤ Others (cont'd)

❖ U.S. tightening of monetary policy

- Need to consider various aspects surrounding tapering: first, both negative and positive signals; second, specific component of capital flow, i.e., equity, bond or banks' borrowing
- Recent trend is different from the past

Capital flow in Korea

(unit: GDP %)

