

Global Financial Safety Nets

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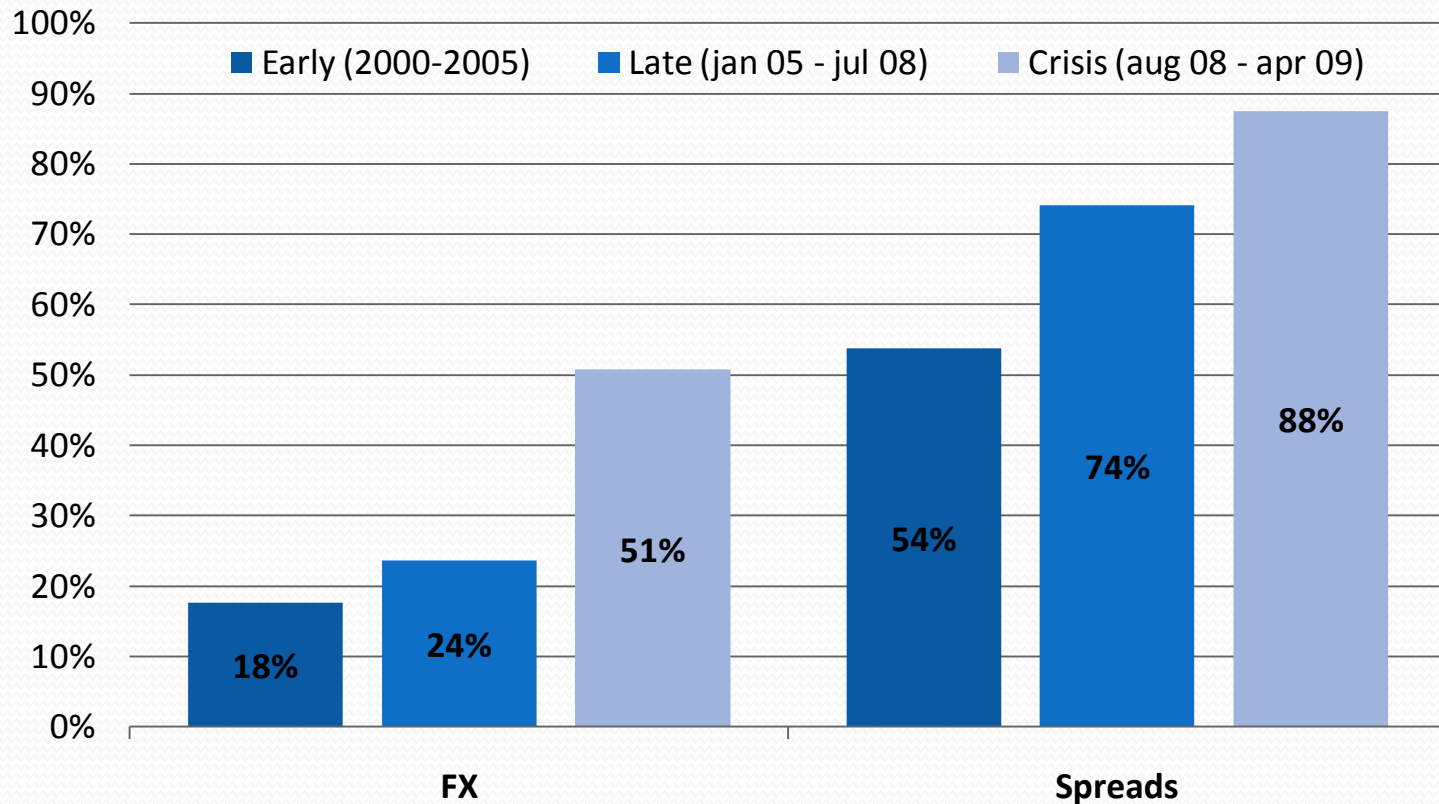
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The priors

- Narrow scope: Global (systemic) shocks
 - Balance sheet concerns may no longer be an issue...but high financial co-movement and excessive FX and spread volatility still are.
- Co-movement severely limits the risk pooling / diversification margin of centralized liquidity provision.
- Current safety nets are useful but inadequate.
- Reserves are here to stay: They reflect leaning-against-the-wind FX intervention, and are not that costly after all.

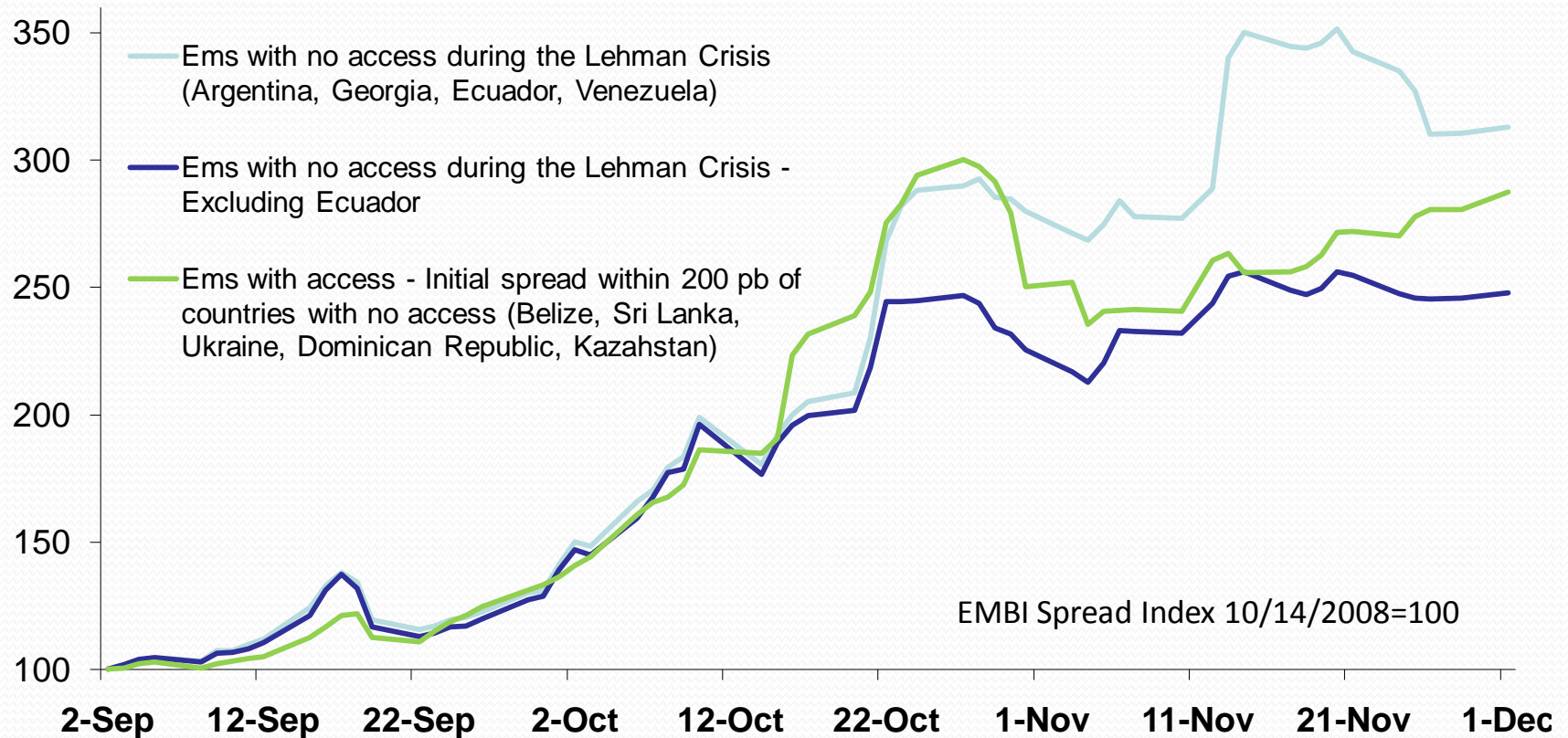
Limited diversification margin

- FX and CDS spread variance explained by 1st PC



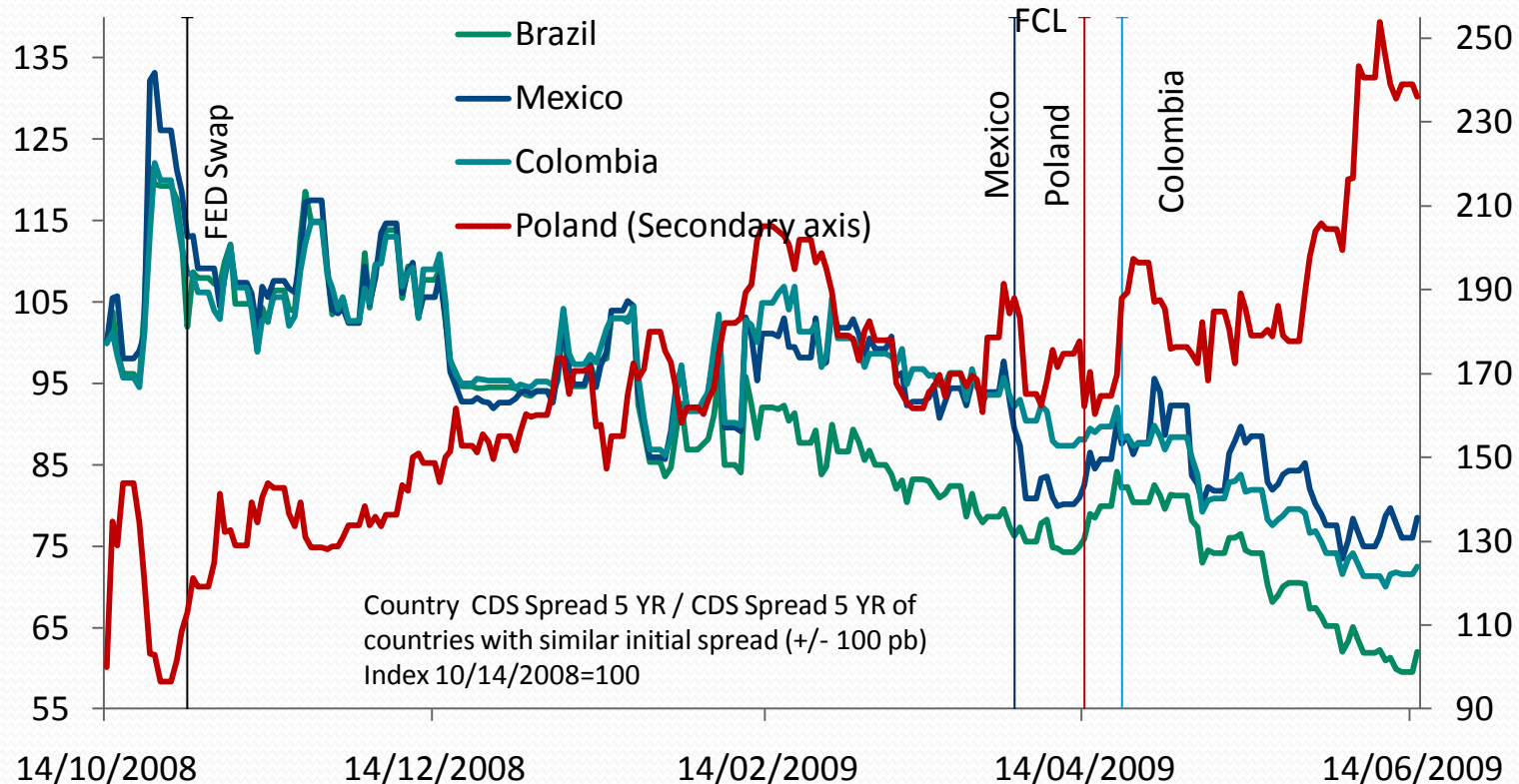
Current safety nets - Lehman

- Effect of access to IMF programs



Current safety nets - London

- Effect of access to liquidity facilities



Brazil (controls): Serbia, El Salvador, Peru, Panama, South Africa, Hungary, Phillipines, Vietnam.

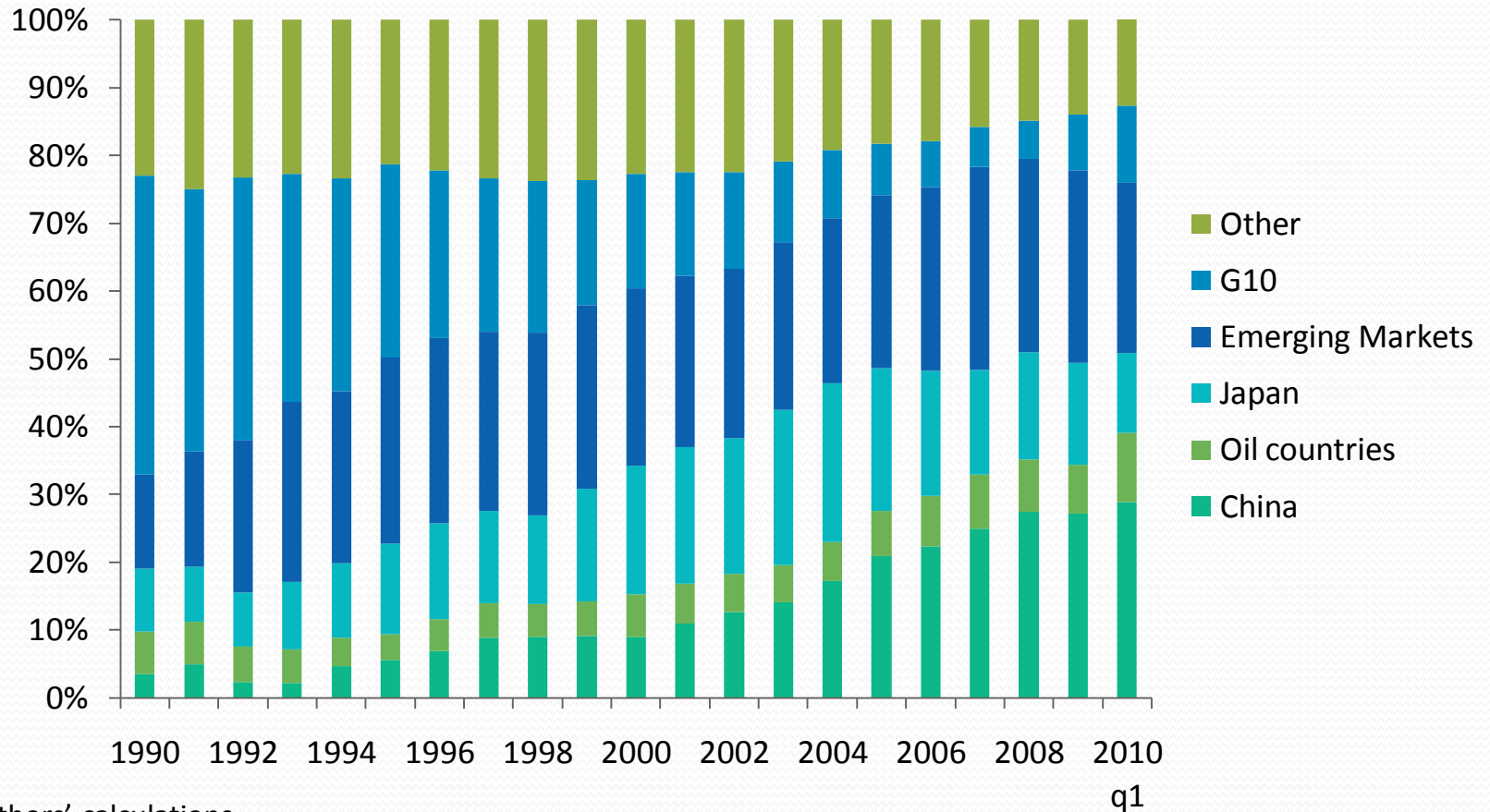
Mexico (controls): Chile, Malaysia, Serbia, El Salvador, Panama, Peru, South Africa, Hungary.

Colombia (controls): Serbia, El Salvador, Peru, Panama, South Africa, Hungary, Phillipines.

Poland (controls): China, Chile, Malaysia.

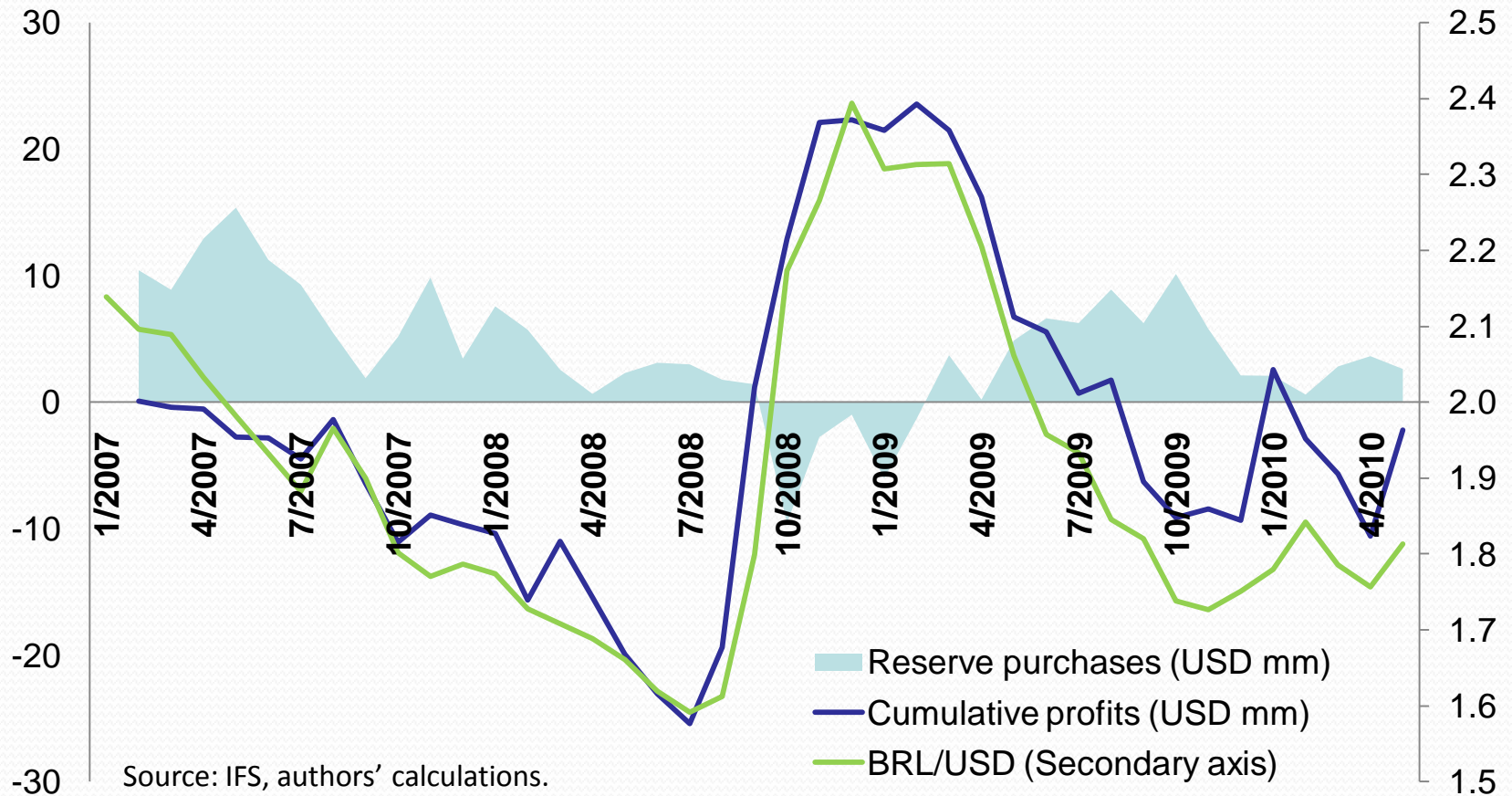
Precautionary reserves?

- International Reserves (% of World Int. Reserves)



Valuation P&L from FX intervention

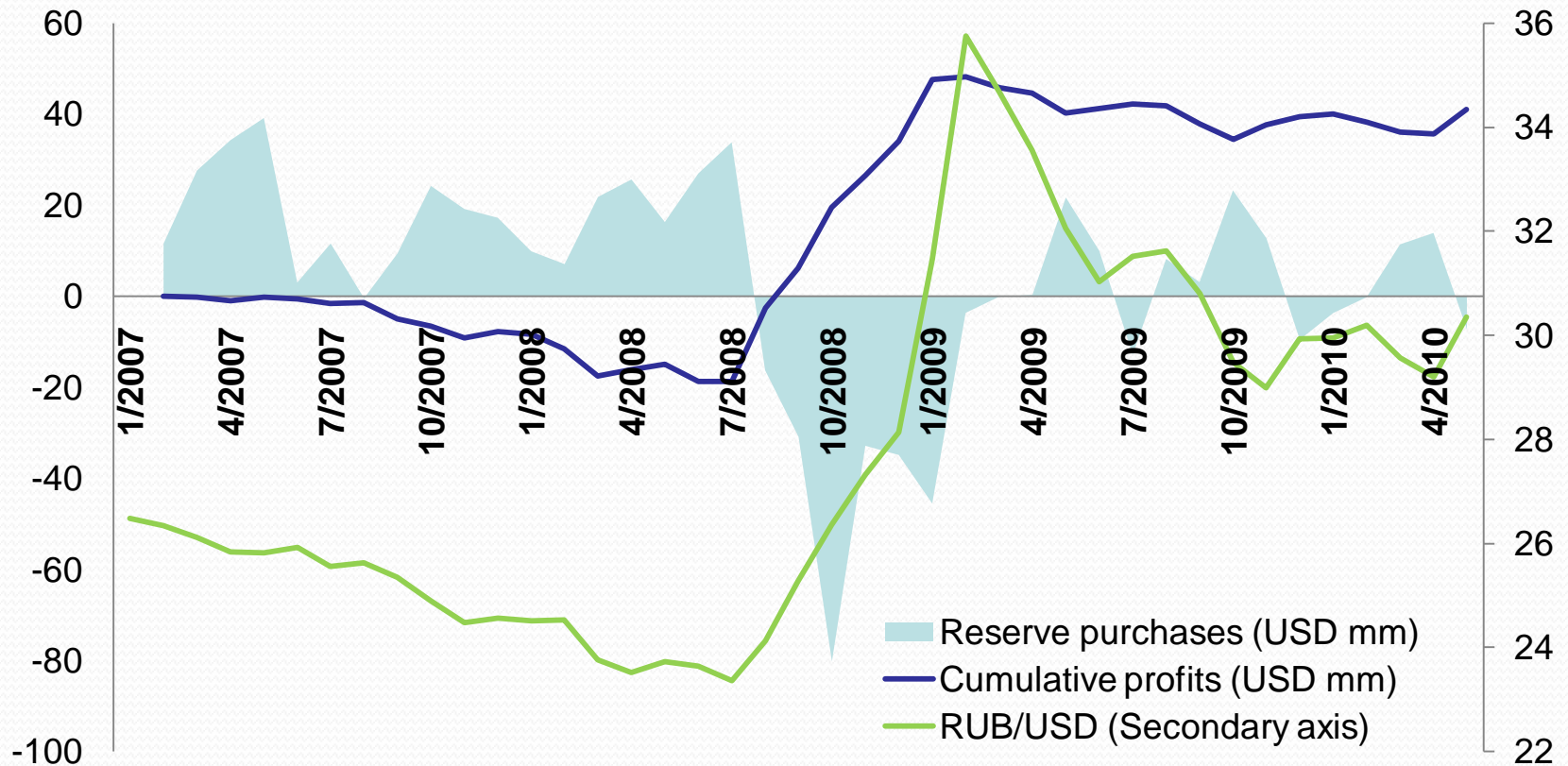
● Brazil



Source: IFS, authors' calculations.

Valuation P&L from FX intervention

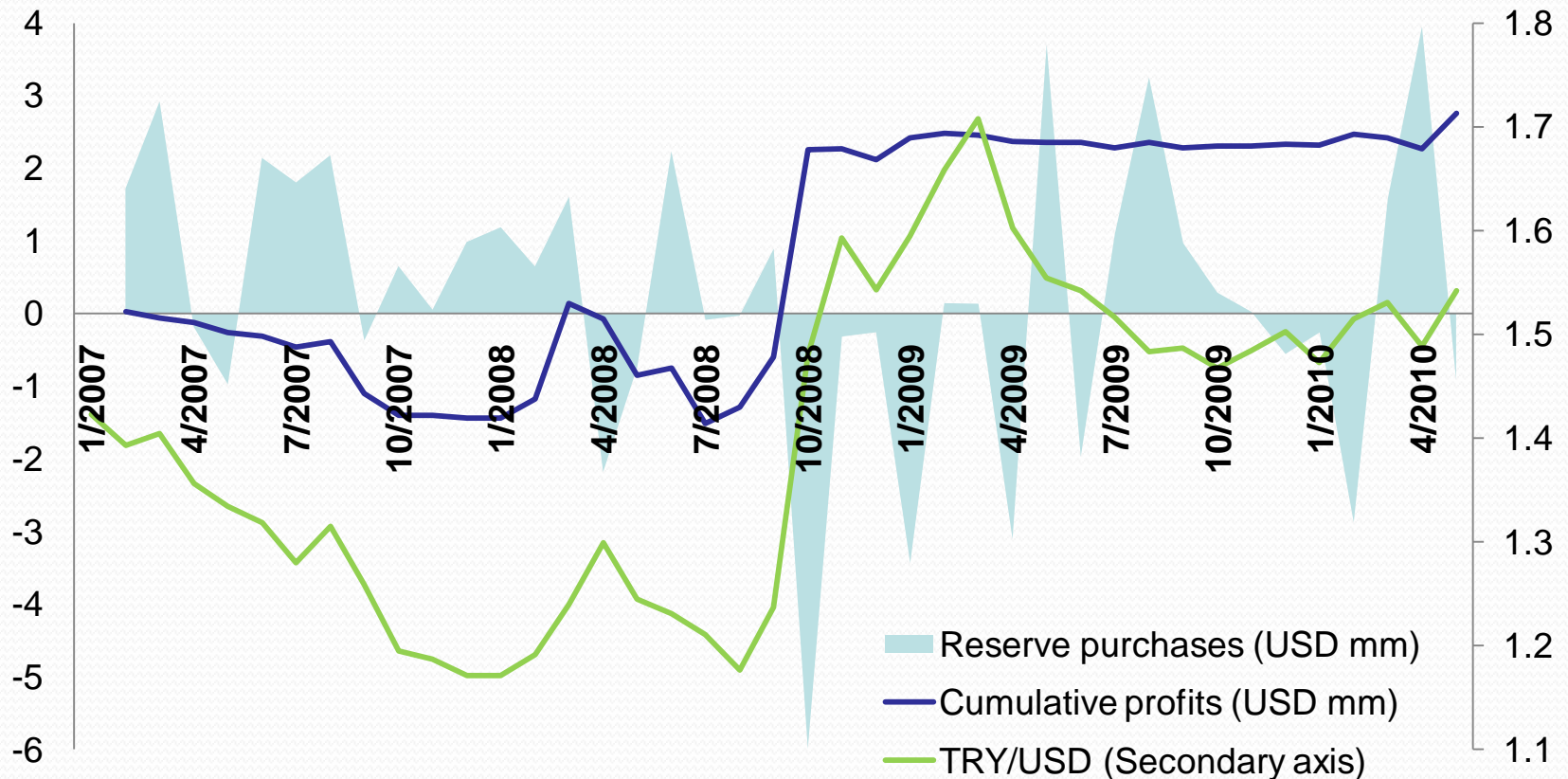
● Russia



Source: IFS, authors' calculations.

Valuation P&L from FX intervention

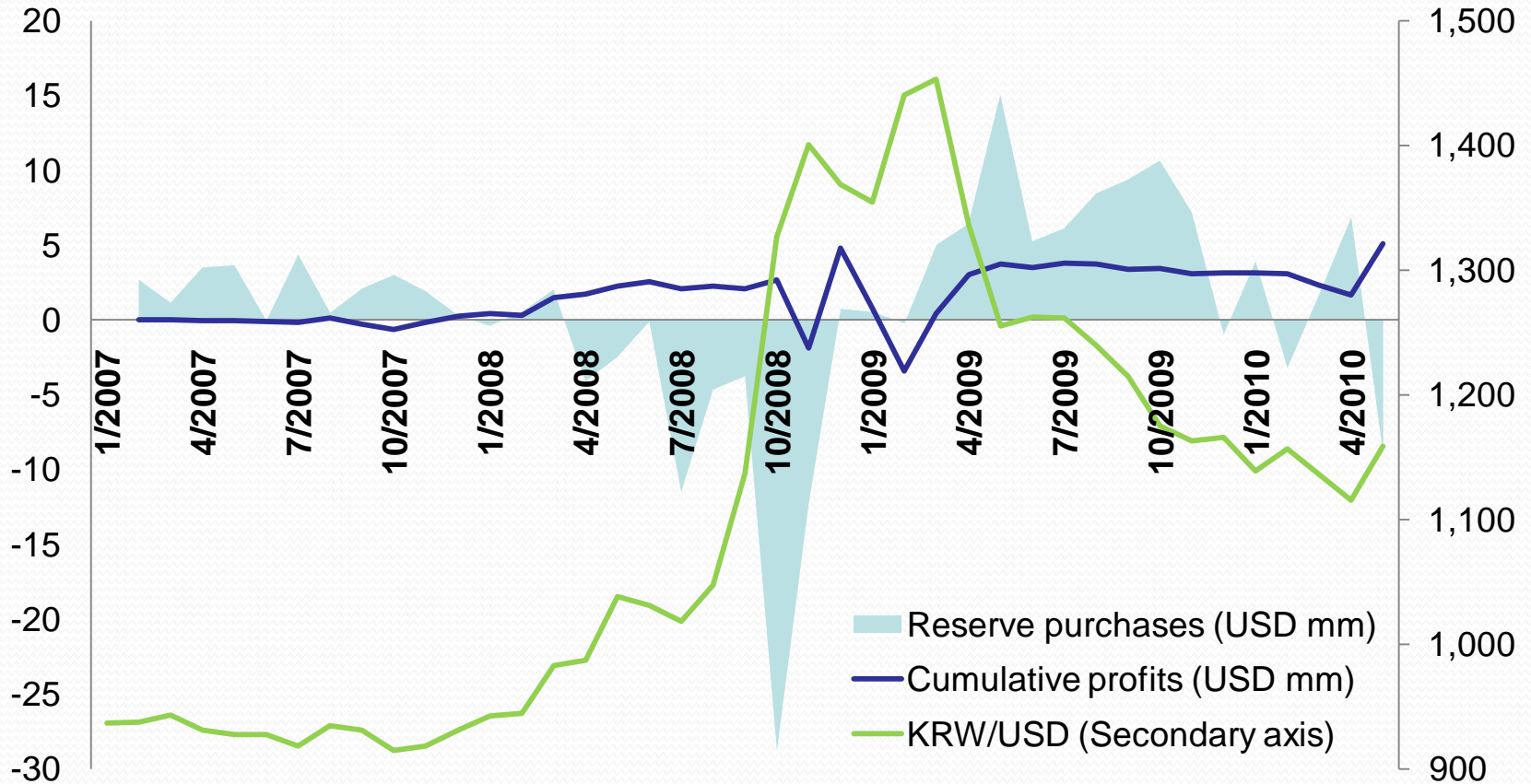
- Turkey



Source: IFS, authors' calculations.

Valuation P&L from FX intervention

- Korea



Source: IFS, authors' calculations.

The principles

- Bagehot's (1873) LLR:
 - Lend **large amounts automatically** (on demand) against **marketable collateral** at **penalty rates** w.r.t. to normal times...
- ILLR → **No collateral**
 - *Large*: Sufficient to meet short-term financial obligations and avoid a collapse...
 - *Automatic*: Non discretionary financial assistance according to **pre-set eligibility conditions**, at a **penalty** relative to program rates.

The new IMF acronyms

- PCL → Extends outreach, under tighter conditions, to non FCL-countries (just a lighter HAPA?)
- GSM → Attract FCL-eligible but indifferent countries in a crisis context
 - Automatic FCL for “systemic” countries
 - SLL: upgrading PCL countries to FCL
- Drawbacks → Uncertainty about GSM activation; no automatic facility for non-systemic countries
 - Would things have been different with the GSM?
- This is probably as far as the IMF can go on its own.

	Stand-By Arrangement (SBA, 1952)	Extended Fund Facility (EFF, 1974)	High Access Precautionary SBA (HAPA, clarified in 2009)	Precautionary Credit Line (PCL)	Short-term Liquidity Line (SLL)	Flexible Credit Line (FCL, 2009)
Availability	Any time	Any time	Any time	Any time	Only in systemic events	Any time
Qualification	No	No	No	Yes, Sound policies	Yes, Sound policies	Yes, Very strong policies
BoP Need	All types of BoP need (including precautionary)	Longer-term BoP needs (structural maladjustments, price/cost distortions, slow growth, inherently weak BoP position)	All types of BoP need; expression of intention not to draw at time of approval	All types of BoP need; absence of actual BoP need required on approval	Special BoP need: temporary, short-term liquidity need from systemic shock	All types of BoP need (including precautionary)
Access	No hard cap (normal limits may be exceeded under exceptional access policy)	No hard cap (normal limits may be exceeded, but high access generally discouraged)	No hard cap (normal limits exceeded by definition and therefore subject to exceptional access policy)	Cap of 1000 percent of quota, with 500 percent cap on approval	Cap to be decided by Board on activation of facility in systemic event based on size of shock and available resources	Uncapped
Exceptional access policy	Yes	Yes	Yes	Yes	Yes	No
Ex post conditionality	Yes. Reviews and PCs	Yes, structural focus. Reviews and PCs	Yes, streamlined. Reviews and PCs	Yes, focused. Reviews only (no PCs)	No	No
Phasing and monitoring	Phased. Quarterly or semiannual reviews depending on circumstances	Phased. Quarterly or semiannual reviews depending on circumstances	Phased. Quarterly or semiannual reviews depending on circumstances	Frontloaded. Up to 500 percent of quota available on approval. Up to additional 500 percent of quota available at start of second year or earlier based on ad hoc review. Semiannual reviews	Frontloaded. Total amount available on approval. No reviews	Frontloaded. Total amount available on approval. Mid-term review to assess qualification only in 2 year arrangements
Arrangement length	Normal length 12-18 months, but up to 3 years if needed. Successor arrangements allowed	3 years. Can be extended to 4 years. Successor arrangements allowed	12 months to up to 3 years. Successor arrangements allowed	Between 1 to 2 years. Successor arrangements allowed	6 months. Up to 1 successor arrangement allowed	One- or two-year arrangements. Successor arrangements allowed
Repayment period	3¼-5 years	4½-10 years	3¼-5 years	3¼-5 years	1¼-2 years	3¼-5 years
Charges, fees	Charges and Fees are as for the SBA for all instruments					

Where do we go from here?

- Back to the domestic LLR analogy → The lender of last resort is the **issuer of last resort (ILR)**
- In the context of a global crisis, ILR are hard to find (Fed, BoJ. ECB? China?)
- A multilateral safety net adds value (avoid carrying costs) only if can leverage on the liquidity created by ILR
- Ultimately, any arrangement would reflect how and to what extent the ILR chooses to channel its assistance

Where do we go from here?

- Stay close to the LLR model → **Multilateral CB swap network**
- The IMF as a facilitator (launching a multilateral manager from scratch appears impractical)
 - Ex ante eligibility through Article IV consultations
 - Purely technical advice (as in the G20 framework) to mitigate the IMF political stigma
- Complementary to reserves (the first line of defense) and regional arrangements if any (the second line).
- Not for everyone but more inclusive and predictable than what the IMF can do on its own.

Thank you