

Foreword

This paper by Professor G. Helleiner was presented to the Commonwealth Finance Ministers at their meeting in Bermuda in September 1996. It contains a rich discussion of recent trends in private capital flows and their impact on economic development with particular focus on problems related to the volatility of capital movements. In analysing these issues, Professor Helleiner brings to the discussion the experiences of a number of East Asian and Latin American countries that have been successful in coping with surges of capital inflows. He reviews their use of a judicious mix of policies that have included exchange rate intervention, monetary sterilisation, fiscal discipline, and a careful use of direct and price based controls on short-term capital flows. The paper also examines the case for capital account liberalisation and the necessary conditions that should prevail before countries embark on full liberalisation.

Professor Helleiner also examines the role of international financial institutions (in particular the IMF and the World Bank) in underpinning the globalisation of capital flows. He emphasises the importance of establishing a workable early warning system; and a credible financing mechanisms that can be deployed quickly and flexibly to assist countries faced with large and sustained capital surges including contagion effects. Professor Helleiner, however, is less enthusiastic about the early amendment of the IMF's Articles of Agreement to promote capital account convertibility for all Fund members. He argues that, notwithstanding the advantages of an opening of the capital account, there would be difficulties in the transition period. He advocates that capital account convertibility must be appropriately sequenced and preceded by policy reforms. He further argues that capital account liberalisation for a great many developing countries has to be seen as a long term process; and that for some countries, which have already liberalised, temporary controls may continue to be an important tool for responding to capital surges which create macroeconomic problems. He concludes that it would therefore, be premature to rush to an amendment of the IMF Articles that commits all members to the achievement of an open capital account. He also suggests that in a globalised world, it is critical that major industrial countries take account of the increased sensitivity to interest rate changes of private capital flows to (or from) developing countries.

Since the paper was written, the issues raised by Professor Helleiner have become even more relevant in the light of the ongoing crises in several East Asian countries. It is my hope that this paper will help to generate debate and assist countries to gain a better understanding of the policy issues involved in managing and coping with private capital flows, both nationally and globally.

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