Why do emerging markets liberalize capital outflow controls? Fiscal versus net capital flows concerns by Joshua Aizenman and Gurnain Kaur Pasricha

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Summary

- EMEs eased controls on outflows in the 2000s in response to a capital surge.
- It tests whether there was a trade-off between earning revenue from financial repression and easing controls to prevent a capital surge.

Capital controls on outflows

This paper asks the following questions for 18 emerging economies from 2001-2010:

- What motivates capital controls on outflows?
- What aspect of capital controls changed since 2001?
- To what exent is fiscal repression a reason for capital controls in emerging economies in the 2000s?
- Regression analysis: Why were controls on outflows eased?
- Event study analysis: What was the impact of easing capital controls outflows on exchange market pressure?
- Was there a difference in easing of controls by inflation targeters vs non-inflation targeters?

Capital controls on outflows

- Early evidence, especially for the 1980s, showed that the main motivation for capital controls on outflows was financial repression.
- More recently capital controls seen as a tool of macroeconomic policy to cope with a capital surge and its implications for reserves, REER, inflation, credit growth, asset prices etc.

How were capital controls on outfows were eased since 2001?

- 2000s did not see much of an increase in restrictions on inflows. It saw more of an easing of controls on outflows.
- Heterogeneity in behaviour: Colombia, Egypt, Mexico, Turkey, all had fewer than 4 net easings in sample, whereas India, Malaysia, Thailand and South Africa had more than 30.
- What were the initial conditions for controls on outflows for these countries?

To what exent is fiscal repression a reason for capital controls in emerging economies in the 2000s?

- This paper finds that EMEs earned negative returns on financial repression during the capital surge of the 2000s.
- The easing was not due to fiscal concerns. So negative returns did not lead countries to ease.
- Question: Why then did they continue with controls on outflows?

Regression analysis: Why were controls on outflows eased?

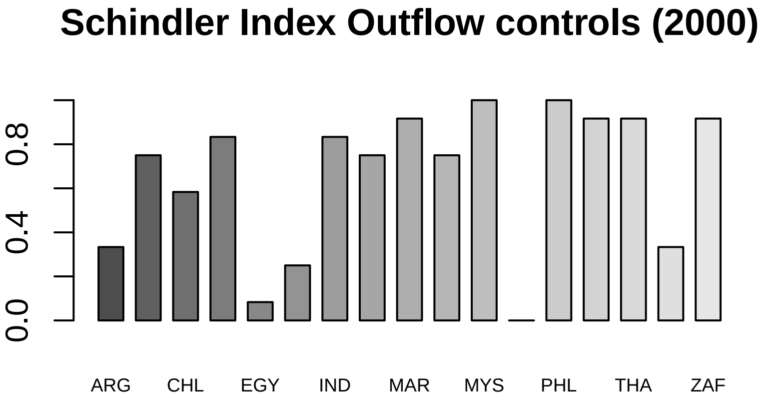
- Easing in response to capital surge and high volatility of net capital inflows.
- Was there a difference in easing of controls by inflation targeters vs non-inflation targeters?
- Are capital controls imposed and eased to hang on to exchange rate pegs?
- The event study finds that easing reduced exchange market pressure.

What motivates capital controls on outflows?

During the 2000s legacy controls on outflows were not tools for financial repression. The paper finds

1. Financial repression gave negative returns.
2. Capital controls were eased in response to a capital surge.
3. So there was no trade-off!

Controls on outflows



My questions

- Explaining easing: Can we include countries like Peru and Turkey that did not have much capital controls on outflows in an analysis to explains easing?
- Measuring trade-off between sacrificing revenues from repression and preventing a capital surge: For countries with negative revenues from financial respression, is there a trade-off?

Suggestions

- Separate section on effectiveness of easing of capital controls on outflows and revenues from repression.
  1. What were the kind of measures that worked?
  2. Details of the event study methodology employed.
  3. Description of data such as EMP measure used, differences across countries observed.

Suggestions

- Interesting question.
- Requires some more clarity on writing.
- More discussion in the four main sections
    1. Measuring financial repression
    2. Why did countries maintain controls on outflows?
    3. Why did countries ease on outflows?
    4. How did inflation targeters differ from non-IT, and exchange rate peggers differ from floaters?

Thank you.