PAPER: "Capital flows and capital controls: the African experience" by Professor C. P. Chandrasekhar

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Some Key Points in the Paper

- A very helpful paper summarizing the various experiences in capital controls and macro-prudential policies.
- Capital controls: measures that seek to directly influence cross-border movements.
- Macroprudential policies: a broad mix of measures that seek to limit foreign exchange exposure: (i) minimize currency mismatch, (ii) prevent exposure to sensitive type of foreign flows, (iii) maintain FX reserves.

African experiences:

i) Tremendous variation in economic development.

ii) In spite of the variation in average income and development, there is significant dependence on commodity exports.

iii) All case studies seem to have concern about the exchange rate, even if they claim to have an inflation targeting regime.

iii) Nigeria and Ghana are interesting given dependence on oil exports.

- They essentially allowed commercial banks to borrow and lend in foreign currency.
- Ghana allowed foreign investors to invest in local stock and money markets.

iv) Ethiopia allows a depreciation of the exchange rate to maintain some stability in real exchange rate.

v) In general, exchange rate and macro-prudential policies appear to be distinct, at least in the African experience.

However, they can be integrated: see Khemraj (2018). I will discuss Prof. Chandrasekhar's paper from a Caribbean perspective and from my research. There is a lot of overlap between the Caribbean and African experiences, in my view.

Excess liquidity in national currency is quite abundant and persistent in Africa and the Caribbean.

Excess Liquid Assets

i) My comments are based on my observations of excess liquid assets and its relation to the exchange rate across the Caribbean and Africa.

ii) I believe understanding the source and persistence of liquid assets can provide a theory for unifying macro-prudential and the exchange rate policies.

iii) Excess liquidity is the product of system of efflux and reflux.

- Government spends from its central bank account (efflux).
- Then, simultaneously the central bank sells a security to the private sector (reflux).
- The central bank can create the security on its liability side just like it creates high-powered money.
- These securities emerge from one-sided sales by the central bank. This point made in our paper on Papua New Guinea in which the one-sided sales appear to stabilize the exchange rate (Direye and Khemraj 2020).
- They replace non-remunerated excess money balances with an interest-earning domestic security.
- They compensate against the holdings of foreign currency assets.
- The excess liquid assets help to stabilize bank portfolio and the exchange rate.

Maintaining Monetary Sovereignty

A non-exhaustive list of possibilities.

i) Do not open the local stock, bond and money markets to foreign capital.

ii) Central bank should create liability-side security like it creates high-powered money.

iii) Reform public accounting to link the consolidated funds with the government's account in central bank.

iv) The largest share of banking should be locally owned.

v) Prevent local banks from accepting deposits and making loans in foreign currency.

vi) Target the exchange rate.

vii) Developing state capacity.

viii) Be aware of ethnic and forms of political mobilization.

Sources

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