No-one left behind? The shortcomings of the Global Financial Safety Net for developing countries during COVID-19

Comments on the Project Paper:

No One Left Behind?

COVID-19 and Shortcomings of the Global Financial Safety Net for low- and middle-income countries

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This view does not represent necessarily the official view of the BCB.

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Project Paper: major points

- Addresses very well the recent inequality among countries to access liquidity in global financial markets;
- GFSN systemically has contributed to financial vulnerability of LICs and low-middle income countries;
- Highlight the interests of the major central banks in the provision of liquidity through swaps
- Points out to the need of more structural measures (as debt relief) than liquidity measures, for LICs in crisis situation
- The GFSN tracker can be very useful to prevent BP crisis
- GFSN reform can push some change in the IMF lending procedures in order to address structural inequalities among countries.

GFSN and FX reserves in EMEs: some considerations

- There is no role for FX reserves in the GFSN as “foreign exchange reserves are national resources in contrast to GFSN resources that are provided from non-national bilateral, regional or global institutions or arrangements”.

- In the theoretical level, “in all types of balance-of-payments crises in EMDEs, the third-party actor must come from outside the country and provide timely, voluminous and smoothly-decided conditionality and decisive action to combat a crisis (Obstfeld 1996)”.

- Consequently, “for crisis prevention and resolution, the fact that crisis finance is provided from outside the country by non-market actors is the major distinction between the GFSN and national foreign exchange reserves.”

GFSN and FX reserves in EMEs: some considerations

- Although FX reserves are national resources, in general, they have been used to maintain/keep the access to global financial markets by the EMEs.

- The main theoretical reference (Obstfeld, 1996) predates the process of reserve accumulation in middle-income and developing economies which started after the consequences of the EMEs crises by the end of 1990s and beginning of 2000s.

- Reserve accumulation by EMDEs can be seen as key development in the global finance sphere in the last decades and has changed the integration for those economies into international financial system, promoting the process of Financialisation. Even LICs have accumulated reserves. For Financialisation in EMEs and changes in central banking, see Painceira (2022)

GFSN and FX reserves in EMEs: some considerations

- In some way, the Fed currency swaps lines have considered EMEs with large reserves, such as Brazil, Korea and Mexico.

- Changes in the global financial system of the last decades, particularly the reserve accumulation in EMDEs, may require a different approach for FX reserves in the Global Financial Safety Net (GFSN);

- Regional Financial Arragements (RFA) for LICs could be reinforced through pool of reserves;

GFSN and Covid crisis: major central banks and cost of liquidity

- Declining role of the IMF and rising importance of the major central banks during the COVID crisis through global instruments;

- New tools of the Fed for monetary authorities during the crisis: Foreign and International Monetary Authorities (FIMA) repo facility.

- Central Banks can use their US Treasuries portfolio holdings in repo operations with the Federal Reserve to mitigate liquidity pressures in US dollar funding markets. More specifically, CBs use their reserves in these operations. The FIMA repo facility became a permanent liquidity tool by July 2021.

- Cost of liquidity facilities matters. It may be useful to highlight this aspect in the GFSN

THE END!