Reserve Bank of India Occasional Papers
Vol. 27, No. 1 and 2, Summer and Monsoon 2006

A Review of Cross-Country Experience in Capital Account Liberalisation

Mohua Roy, Rekha Misra and Sangita Misra*

The paper reviews the experience of select countries - both advanced and emerging markets - in regard to capital account liberalisation (CAL). The advanced countries' experience with regard to CAL is analysed with special focus on the sequencing of CAL. The move towards CAL by many of the emerging market economies (EMEs) during the 1980s and the circumstances that led to some policy reversals and the subsequent change in the mainstream thinking during the 1990s have also been analysed. The paper also presents some of the extant capital account restrictions in select advanced countries and EMEs, emanating from security and prudential considerations that have come to be accepted as being consistent with a framework of full capital account liberalisation. Finally, the paper draws some lessons from the cross-country experience, particularly in regard to the need for sound economic policies and effective risk management strategies, prudential supervision and proper reporting standards to meet the emerging challenges of CAL.

JEL Classification : F21, F31, F32

Keywords : Capital Account Liberalisation, Capital controls, Capital flows, Emerging Market Economies

Introduction

Capital account liberalisation (CAL) was undertaken over a period of years in advanced countries, including the euro area, particularly after the breakdown of the Bretton Woods system of fixed exchange rates in the mid-1970s. During the 1980s and 1990s, many of the emerging market economies (EMEs) also undertook capital account liberalisation. This

* Dr. Mohua Roy is Director, Monetary Policy Department, Smt. Rekha Misra and Smt. Sangita Misra are Assistant Adviser and Research Officer, respectively, in the Department of Economic Analysis and Policy (DEAP). This is a modified and expanded version of a paper presented to the Committee on Fuller Capital Account Convertibility (CFCAC). The paper was prepared under the overall guidance of Shri S. S. Tarapore, Chairman, CFCAC, Shri K. Kanagasabapathy, Secretary, CFCAC and Dr. R. K. Pattnaik, Adviser, DEAP. The views in this paper are those of the authors and not necessarily of the institution to which they belong.

was followed by episodes of huge capital inflows into some of these countries, the magnitude of which became unmanageable and destabilising for many EMEs. Based on the cross-country experience in capital account liberalisation, especially since the East Asian crisis of 1997, the mainstream thinking both at academic and policy levels has changed in the recent years. Against this backdrop, the purpose of the paper is to examine the experience of select major countries which went in for CAL and draw lessons from their experience with particular focus on (i) the nature of capital controls by advanced countries during the phase of run up to capital account liberalisation; (ii) the kind of controls and safeguards retained by even fully liberalised regimes; and (iii) the circumstances leading to policy reversals by some EMEs in the post-1997 build-up of the crisis-ridden international economic and financial markets scenario. Section I gives a brief account of the evolution of capital account liberalisation in the global context. Section II elaborates upon the advanced countries' experience with regard to capital account liberalisation with special focus on the sequencing of CAL. Section III analyses the experience of emerging market economies (EMEs). Section IV attempts a presentation of extant capital account restrictions in select advanced countries and EMEs. Section V draws some important lessons from the cross-country experience.

Section I

Evolution of Capital Account Liberalisation

Tracing out the history of capital account liberalisation, one observes that the period since 1870s till the outbreak of the World War I, was a period of *laissez faire,* with no capital controls. This period was marked by a boom in international flows of goods, labour and capital across nations, both developed and developing. Most of the foreign investment during this period was long-term and was mainly directed towards infrastructure, especially utilities and railroads. The boom ended with the onset of World War I. The ensuing years from 1920 to 1931 saw a modest revival of capital flows, mostly to emerging market economies to meet their developmental needs.

The post-World War II period from 1945 was marked by imposition of capital controls by most economies. Even the developed countries maintained controls for prolonged periods after World War II driven by a range of motives including exchange rate policy, monetary policy and tax policy considerations. As a result, capital flows remained marginal. Capital controls, till the early 1970s, were rather considered as an integral element of the fixed exchange rate regime of the Bretton Woods system.

Capital account liberalisation became more common after the breakdown of the Bretton Woods system of fixed exchange rates in the mid-1970s. In tandem with several countries gradually switching over to varied forms of floating exchange rates, these countries also liberalised their controls on capital flows. The generalised move towards CAL in the 1980s in the advanced countries coincided with a general shift towards more market-oriented economic policies aimed at achieving non-inflationary growth together with a gradual move towards multilateral frameworks such as the Organisation for Economic Cooperation and Development (OECD) and the European Union (EU). Notwithstanding certain periods of market disruption and speculation in the post-CAL period, there were no cases of serious policy reversals leading to reimposition of capital controls by the advanced economies.

Many EMEs in Latin America as also Asia embarked upon capital account liberalisation from the early 1980s. This period was, in general, oriented positively towards opening the capital account and in a world fast integrating through both trade and financial flows, capital controls were increasingly perceived as ineffective and even distortionary. Consequently the volume of capital flows into the developing economies accelerated till the mid-1990s. The general fear associated with CAL is the outflow of capital, but the opposite has also been the case in certain economies, *viz*., Chile and Malaysia. With the magnitude of capital flows becoming unmanageable and destabilising for the EMEs and sterilisation operations getting increasingly ineffective, some of the EMEs backtracked from the liberal capital account measures and imposed restrictions – both price and non-price based measures. While some EMEs faced the challenge of managing increased inflows, some other EMEs experienced sudden stops and reversal of flows that led to a series of crises during the mid-1990s. This opened a whole new debate and a plethora of literature on the timing, sequencing and the pace of CAL globally.

As a result of these developments, the mainstream thinking in both academic and policy-making circles turned somewhat less enthusiastic about the benefits of capital account liberalisation, particularly before meeting several prerequisites in terms of strong macroeconomic policy framework and soundness and efficiency of the financial system and markets. The IMF also shelved its proposal of 1997 for making capital account convertibility as an obligation for its members, and has been following the practice of appropriately advising its members in a country-specific context to follow generally a cautious, gradual and carefully sequenced process of capital account liberalisation.

The advanced countries had, no doubt, some intermittent controls on capital flows during the phase of liberalisation, but did not substantially reverse policies away from a liberal regime, whereas a widely observed feature about EMEs was the reversal of policy towards CAL and reintroduction of controls in the wake of capital account crises. Nevertheless, some forms of capital controls are prevalent even in liberalised regimes, more prominently in respect of direct investment, real estate transactions, and transactions in capital and money market securities. Such regulatory safeguards, emanating more from security and prudential considerations, have come to be accepted as being consistent with a framework of full capital account liberalisation.

Section II

Experience of Advanced Countries

Most advanced countries liberalised their capital account over a period of about two decades from 1974 to 1994. The period of transition, however, varied between countries ranging from a number of years in respect of France and Japan to a few months in the case of United Kingdom. Australia and New Zealand are also examples of speedy transition from a rather restrictive to open regimes. Experience of these countries reveals that accompanying macroeconomic policies and domestic financial sector reforms were critical for successful liberalisation. In particular, the need for developing adequate prudential supervision standards has been underscored. In most cases, direct investment flows were formally liberalised ahead of portfolio flows. On the other hand, restrictions on cross-border bank lending and foreign investment opportunities by the residents were among the last to be lifted.

The US was the first country that went in for complete capital account liberalisation (CAL) in 1974. Between 1979 till 1991, most of the European countries, Japan, Australia and New Zealand also adopted full capital account liberalisation although patterns as well as the time taken varied between the countries.

United States

The United States, that had generally adopted liberal policies with regard to capital account in the post-war period, introduced capital controls on account of speculative outflows in the 1960s. Controls in the form of Interest Equalisation Tax (1963), Voluntary Guidelines limiting foreign lending and investment (1965) and Voluntary Guidelines limiting foreign direct investment (1968) were introduced. Most of these controls were eliminated from 1974 onwards after the breakdown of the Bretton Woods system. Since then, the United States has followed a liberal capital regime with limited controls mainly pertaining to security concerns (Bakker & Chapple, 2002).

Europe

Unlike the United States, the move towards capital account liberalisation amongst European countries was marked by alternate phases of controls and relaxations and has ranged over one and a half decade (UK liberalised in 1979, while Greece in 1994). Most of the European countries tried to limit the inflows during the late 1960s, first by indirect measures aimed at discouraging non-residents from acquiring domestic assets and eventually through direct capital controls. Even some of the liberal European countries such as Germany and Switzerland tightened their exchange control regimes. Most controls on inward flows were lifted in 1970s, when the appreciation of European currencies and Japanese yen *vis-à-vis* dollar was eventually accepted and the Bretton Woods fixed exchange rate system gave way to a regime of flexible exchange rates. In the period subsequent to the first oil crisis of 1973, many of these countries experienced downward exchange rate pressures and, hence, imposed restrictions on outward capital flows. These restrictions continued throughout the 1970s. In the 1980s, many of the European countries again developed strategies to dismantle their control systems. This coincided with significant progress towards European integration, which later culminated in monetary unification.

Other Countries

Outside Europe, Japan, Australia and New Zealand have also imposed controls on short-term capital flows for extended periods. Japan's approach towards capital account remained inconsistent till 1979, with controls imposed and subsequently eased in 1967, 1973 and 1979. As a result, investment inflows generally remained low. Subsequently, Japan followed a very gradual approach towards liberalisation ranging over a decade from 1979 to 1991. Australia and New Zealand, on the other hand, are examples of rapid move to capital account liberalisation. On the back of the foreign exchange crisis of 1984, New Zealand liberalised all restrictions within a year (mid-1984 to mid-1985). Prior to the move, New Zealand followed a regime of pervasive capital controls, exchange rate peg and import controls on a wide range of products. The chronological pattern of CAL in advanced countries is presented in Table 1.

Table 1: Abolition of Capital Controls – Developed Countries

Country	**Year of abolition of capital controls**
United States	1974
European countries	
United Kingdom	1979
Germany	1981
Netherlands	1986
Denmark	1988
France	1990
Sweden	1989
Italy	1990
Belgium	1990
Austria	1991
Finland	1991
Spain	1992
Portugal	1992
Ireland	1993
Greece	1994
Japan	1991
Australia	1985
New Zealand	1985

Source: Bakker and Chapple (2002) and IMF *Annual Report on Exchange Arrangements and Exchange Restrictions,* various issues.

The process of CAL is covered in some detail for two countries, *viz.*, France and the United Kingdom, in the following paragraphs[2].

France

Background

France followed a very gradual approach towards CAL during the 1980s. In 1979, France joined the European Monetary System (EMS) while maintaining a relatively tight set of capital controls. Subsequent to the second oil price shock later in the year, France entered into a recessionary phase. The Government resorted to expansionary policies. The nationalisation of the financial sector and the subsequent increase in the government control of the banking sector up to 85-90 per cent eroded the confidence of the markets resulting in considerable outflows. A series of speculative attacks on the exchange rate forced devaluation of French franc by over 25 per cent during 1981 to 1983. Capital controls were further tightened. Measures included prohibiting all forward transactions by importers and exporters and steps to prevent evasion by using leads and lags in current account transactions. However, controls failed to be effective especially with large external imbalances. Besides, controls involved real economic costs.

Policy Response

A major reorientation occurred in French economic strategy in 1983. This involved deregulation in the financial sector, which was brought about in stages. The public debt market was reformed to enhance the investors' interest. Quantitative credit control mechanism was abolished in 1985. While this well-planned liberalisation of financial sector was being implemented, France continued to maintain capital controls. When the French macro-economic situation strengthened, current account stabilised in 1984 and the financial sector was considered to be able to withstand foreign competition, capital controls were withdrawn gradually. The details of the capital account liberalisation process in France are given in Table 2.

---

[2] The discussion is based on Bakker and Chapple (2002).

Table 2: Chronology of Key Changes in Capital Account Controls in France

1980 July	L Relaxation of restrictions on inward and outward direct investment.
1981 May	T D*evises-titres* market, limitations on leads and lags in trade settlements, and limitations on direct investment abroad reintroduced.
1982 March	T Further restrictions on surrender of export proceeds and on direct investment abroad introduced.
1983 March	T Further foreign travel allowances reduced, a ban on use of personal credit cards abroad, and *carnet de change* (a booklet in which foreign exchange purchases were recorded) introduced.
December	L Limits on foreign travel allowances and foreign direct investment eased. L C*arnet de change* abolished.
1984 July	L Ban on use of personal credit cards abroad abolished.
November	L Controls on direct investment abroad eased.
1985 February	L Inward direct investment originating from non-EEC countries eased.
April	L Eurobond issues denominated in French francs authorised.
September	L Financing rules for outward direct investment outside the European Community eased.
December	L Regulations for outward portfolio and direct investment eased.
1986 January	L Foreign travel allowances eased.
April	L Requirement of prior authorisation of direct foreign investment eliminated.
May	L D*evises-titres* market abolished, purchases of secondary residences abroad liberalised, forward foreign exchange operations eased, and authorisation procedures for direct investment abroad eased.
November	L Bank lending in French francs to non-residents partially liberalised. L Administrative control through commercial banks of import and export settlements abolished (*domiciliation* regime).
1987 May	L Exchange controls for commercial enterprises substantially eased. L Trade in gold liberalised.
July	L Limits on tourist travel allowances abolished.
1988 June	L Domestic enterprises permitted to operate foreign currency accounts. L Restrictions on borrowing abroad abolished.
1989 March	L Bank lending in French francs to non-residents fully liberalised.
June	L Commercial banks' foreign exchange positions liberalised. L All residents were granted permission to open ECU-denominated accounts.
1990 January	L All remaining exchange control regulations abolished (Decree 89/938).

T: Tightening of controls; L: Loosening of controls

Source: Bakker and Chapple (2002)

Assessment

The overall liberalisation process spanned over a period of 6 years – 1984-1990. During 1986-87, there was some disruption in the forex market, which led to some realignment when the French franc was devalued by about 3 per cent. There were sizable increases in portfolio flows into France (from below 0.5 per cent of GDP in early 1980s to close to 4 per cent of GDP by late 1980s). Yet, the liberalisation efforts continued uninterrupted till 1990 when France adopted complete CAL. The French exchange rate was again tested by the markets during the 1992-93 EMS crisis. It led to decisive interest rate hikes, heavy interventions and broadening of the EMS fluctuation margins, though the central rate of the French franc was not adjusted. There was no reversal with regard to capital account measures. Eventually, French franc joined the Euro on January 1, 1999. Notwithstanding the fact that peer pressure (in terms of the prospect of further European economic and financial integration) has been a major driving force behind French liberalisation of capital movements, the experience of France remains commendable with respect to its integrated approach to reform involving macroeconomic stabilisation and institutional strengthening. Deregulation of financial markets, abolition of quantitative credit controls, industrial policy reforms and discontinuation of subsidies were undertaken before adopting full CAL. The French approach to strengthen the domestic economy before liberalising the volatile items in the capital account was the key element behind the French attempt at CAL.

United Kingdom

Background

United Kingdom's experience is a classic case of rapid liberalisation of capital controls. Since World War II till 1979, UK operated one of the most extensive system of capital controls along with tight domestic financial regulation. Despite controls, UK faced frequent exchange rate crises and poor economic performance. The first such crisis was in 1967 when sterling came under downward pressure on account of unloading of official sterling balances with pound sterling becoming less important as a reserve currency. A second sterling crisis in November 1976 led to additional tightening of capital controls (Table 3). The second oil price shock in 1979 resulted in considerable upward pressure on sterling.

Table 3: Chronology of Key Changes in Capital Account Controls in UK

1958	December	L Convertibility of sterling introduced.
1961	July	T Introduction of restrictions on direct investment outside sterling area.
1967	April	L Restrictions on repatriation of non-residents' capital eased.
1971	August	T Controls on portfolio inflows introduced.
	December	L Controls on portfolio inflows abolished.
1975	July	T Postponement of capital controls *vis-à-vis* EEC members.
1976	November	T Imposition of restrictions on banks' financing trade between countries other than the United Kingdom, conversion of foreign currency bills into sterling by banks no longer permitted.
	December	T Tightening of the monitoring of sales of foreign currency for sterling.
1977	October	L Restrictions on sterling borrowing to fund inward direct investment and also on travel allowances for residents eased.
	December	L Capital outflows to other EEC countries eased.
1978	June	L Restrictions on resident institutional investors investing in foreign currency securities eased.
1979	January	L Abolition of restrictions on sterling lending to non-resident–controlled companies operating in the United Kingdom.
	June	L Restrictions on outward capital flows eased.
	July	L Abolition of all restrictions on outward direct investment and significant liberalisation of outward portfolio investment.
	October	L Suspension of the Exchange Control Act of 1947 and removal of all remaining barriers to inward and outward flows of capital. L Remaining exchange controls abolished.

T: Tightening of controls; L: Loosening of controls
Source: Bakker and Chapple (2002)

Policy Response

The initial response was to intervene in the market to counter upward pressure, but because of the overshooting of domestic monetary aggregate targets, the exchange rate was allowed to seek its own level. The sterling appreciated substantially during 1979 in nominal effective terms, thus raising concerns about competitiveness and deterioration of non-oil current account. These developments, together with comfortable foreign exchange reserves, nullified the arguments favouring capital controls and created the platform for CAL. The government also recognised that the abolition of capital controls had to be accompanied by domestic deregulation and macro-economic policies oriented towards stabilisation. High level of domestic cost increases was a cause of concern enunciating the need to break the wage price spiral to ensure that benefits are not lost through loss of competitiveness.

Partial relaxation was undertaken in June 1979. This also marked the beginning of further domestic deregulation and enhancement of market forces. Remaining restrictions were abolished in one step in October 1979. Measures were undertaken to remove direct credit control measures and improve the functioning of the labour market.

Assessment

Though the process of liberalisation of capital controls in UK was one of the fastest, it was part of a broader policy framework aimed at improving the functioning of the overall UK economy in late 1970s. While inflows increased marginally, the immediate post-liberalisation period saw a substantial hike in capital outflows from UK. Economic growth in UK improved during the 1980s and inflation fell. Towards the end of 1980s, UK witnessed a period of industrial unrest and an asset price bubble developed. The exchange rate remained volatile at times though there was no backtracking towards capital control measures. UK at present has no restrictions on capital transactions in money, capital and derivatives market and with respect to personal capital transactions and institutional investors. The authorities have, however, retained the power to impose restrictions on inward direct investment if it hinders national interest.

A chronology of key changes in capital controls in the United States, Japan, Australia and Italy is provided in Annex 1.

Section III

Emerging Market Economies' Experience

The decade of 1980s and 1990s saw a range of pressures on developing countries to open up to foreign capital flows triggered by the fast global integration of trade and finance. Many emerging market economies like Malaysia, Indonesia and Thailand maintained unrestricted capital accounts in the 1980s and till the mid-1990s. This was followed by episodes of huge capital inflows into these countries particularly in the 1990s, the magnitude of which became unmanageable and destabilising. Sterilisation operations were usually the first policy response, but, such operations typically entailed costs to the central banks and attracted further inflows as they tended to keep interest rates high. Recognising the limitations of sterilisation operations beyond a point and succumbing to the appreciation pressures due to huge inflows, some of these emerging economies reversed from the liberal capital account and re-imposed restrictions – both price and non-price based – around the crisis periods.

The literature on crisis experiences of EMEs shows that the risks of CAL arise mainly from inadequate preparedness before liberalisation in terms of domestic and external sector policy consolidation, strengthening of prudential regulation and development of financial markets, including infrastructure, for orderly functioning of these markets (Kawai *et al,* 2003). In this context, the East Asian experience and that of some Latin American countries is of relevance.

Mexican Crisis

The Mexican crisis in 1994-95 first drew attention to the volume and velocity of the flows involved in capital account crises in emerging market economies. From the late 1980s to the early 1990s, Mexico liberalised its capital account as part of a larger program of economic stabilisation and reform, internationalisation of the stock market and liberalisation of FDI. During 1987-93, Mexico achieved reduction in inflation from 160 per cent to 8 per cent (partly through a wage and price freeze), economic growth which stagnated in the 1980s rose to 3 per cent in 1989-93, external debt was restructured and private capital inflows surged, contributing to a large increase in international reserves. Between 1990 and 1993, Mexico received more than $ 91 billion in net capital inflows; 67 per cent of this or $ 61 billion was portfolio investment (Folkerts-Landau and Ito, 1995). There were, however, weaknesses in Mexico's economic position including current account deficit at 6.5 per cent of GDP in 1993, financed largely by short-term capital inflows, a steep real appreciation of the *peso* and a major deterioration in the private sector's saving performance. Mexico's weak external position was exacerbated in 1994 by a substantial rise in world interest rates, which prompted international investors to reassess the share of their portfolios invested in emerging markets. All these developments tended to weaken the *peso*. The *peso* was allowed to depreciate within its band, but the vulnerability of the economy was increased by the replacement of *peso*-denominated government debt by Tesobonos, instruments indexed to the U.S. dollar. The current account deficit widened further to 8 per cent of GDP for 1994. All these factors contributed to the eruption of the crisis in December 1994. Though a devaluation of the *peso* occurred immediately and the *peso* was allowed to float after a massive loss of international reserves, it did not restore confidence and the *peso* continued to depreciate sharply, as financial markets were suspicious about Mexico's ability to service its short-term debt (Martinez, 1998).

East Asian Crisis

The East Asian region was characterised by high rates of growth since the 1980s which had accelerated to a range of 7 to 10 per cent in the 1990s accompanied by high investment rates which averaged around 30 per cent through the 1980s (except in the Philippines) and kept well above 30 per cent of GDP and above 40 per cent in Malaysia and Thailand in the 1990s. There were moderate deficits in the general government budget ranging between 0.3 per cent of GDP and 3 per cent of GDP. Malaysia recorded deficit of 4 per cent of GDP during the 1980s, but rapidly consolidated its position and moved into fiscal surplus since 1994. Thailand recorded fiscal surpluses all through the 1990s (Rangarajan and Prasad, 1999, Patra *et al*, 1999 and Bhalla, 1998).

The East Asian economies faced a serious currency crisis during 1997-1999. It began in Thailand without much early warning signals in late June 1997 and afflicted other countries such as Malaysia, Indonesia and South Korea, and lasted upto the last quarter of 1998. It came as a surprise, not only because of the large number of countries affected and the speed of the spreading crisis from one country to another, but also because of the fact that before the crisis many countries had been showing healthy signs: long periods of impressive growth rates, responsible government fiscal policies, and steady investment in human and physical capital. Prior to the crisis, there was a boom in private capital flows to emerging markets in the 1990s, which rose to around $ 300 billion at the time of the East Asian crisis in mid-1997. Some countries allowed entry of this inflow in a completely controlled manner (China, India) while others (e.g. Thailand, Malaysia, Indonesia) had varying degrees of controls. The restrictions on outflows also varied among the countries. None of the emerging markets, however, had a fully floating exchange rate. Central banks intervened to restrict movements in exchange rates and most of them sought to keep the exchange rate under an implicit or explicit peg or a band. The choice of fixed exchange rate regimes was predicated by the costs and ineffectiveness associated with sterilisation, the lack of scope for any further fiscal consolidation, the limit on monetary tightening that would have encouraged further inflows and the erosion in competitiveness which would have occurred under greater exchange rate flexibility.

The saving rate which had stabilised around 30 per cent in most of the countries in the 1990s was not sufficient to finance the high rates of investment. As foreign borrowing rates were almost 3 to 5 per cent less than risk-free domestic deposits, excess borrowing occurred. The widening saving-investment gap was reflected in large and persistent current account deficits (CAD) during the 1990s when Thailand and Malaysia had CAD at 8 per cent of GDP and 10 per cent of GDP, respectively, in 1995. In Indonesia, there was a worsening of the current account deficit in 1995 to 3.3 per cent, after the relatively modest levels during the immediately preceding years. In the Philippines, the current account deficit stabilised at a high of around 4 to 5 per cent. There was a marginal upward movement in inflation during the 1990s in all the economies although the rates remained modest. Philippines experienced a reduction in its inflation rate from over 15 per cent during the 1980s to around 8 per cent in 1995-96.

Fixed nominal exchange rates acted in conjunction with worsening current account imbalances and positive inflation differentials to produce real appreciation of the currencies. Other factors also contributed to currency overvaluation and loss of competitiveness such as the rapid appreciation of the US dollar after 1995, the nominal devaluation of 50 per cent of the Chinese yuan in 1994 and the slump in external demand. Taking 1990 as the base year, the real exchange rate appreciated by 19 per cent in Malaysia, 23 per cent in the Philippines, 12 per cent in Thailand and 8 per cent in Indonesia in 1997. The ratio of debt stock (including short-term debt) to reserves, indicating solvency, showed that except Indonesia and the Philippines for whom this ratio was 267 per cent and 166 per cent, respectively, other Asian economies were well below 100 per cent. The share of short-term debt to total debt varied between 13 per cent (in Philippines) and 32 per cent (in Thailand). In retrospect, the key weaknesses were the large inflow of short-term capital, and the fact that most of the affected countries had high current account deficits and overvalued exchange rates.

The crisis left a trace of heavy economic and social costs. These Asian economies saw an overall decline in 1998. Gross Domestic Product (GDP) in 1998 contracted almost 6 per cent in Korea, 8 per cent in Thailand and 7 per cent in Malaysia. Social unrest and political uncertainty compounded the economic and financial dislocations in Indonesia to reduce real GDP by almost 14 per cent. Excepting Indonesia, all the economies showed a positive growth rate in 1999 as they recovered with international support and domestic policy improvements. This episode was, however, a major shock to countries embarking upon rapid capital account liberalisation and raised doubts about the benefits of liberalisation of capital account without certain macroeconomic and prudential policy prerequisites. The major macroeconomic causes for the crisis were identified as: current account imbalances with concomitant savings-investment imbalance, overvalued exchange rates, high dependence upon potentially short-term capital flows and huge portfolio flow composition of foreign investment. These factors were exacerbated by maturity mismatches, currency mismatches, moral hazard behaviour of lenders and borrowers, excessive leveraging, herd behaviour of markets and predatory speculation, and the sharp appreciation of the US dollar. The crisis period witnessed reversals of policies towards capital account by these countries. Such policy changes in select countries are discussed in some detail in the succeeding paragraphs.

Malaysia[3]

Malaysia, which had generally been an open economy, saw a temporary episode of imposition of controls and its subsequent elimination during 1994. A substantial backtracking from capital account liberalisation occurred during 1997. To avoid appreciation of the ringgit, the initial policy response to heavy inflows in Malaysia in 1994 was for the central bank to intervene in the forex market by buying up foreign exchange and thereafter to sterilise the excess domestic liquidity. With sterilisation becoming costly (with shortage of government paper) and ineffective (sterilisation operations kept interest rates high, which in turn attracted capital inflows), the authorities introduced a number of direct and regulatory capital control measures in early 1994. The measures were specifically designed to limit short-term capital inflows. Specific measures were:

- Residents were prohibited from selling Malaysian money market securities to non-residents;
- Commercial banks were prohibited from engaging in non trade-related bid-side swaps or forward transactions with non-residents;
- Asymmetric open position limits, that is, ceilings on banks' net liability positions excluding trade-related and foreign direct investment flows, were imposed, aimed at curtailing bank foreign borrowing to engage in portfolio or non-trade transactions; and
- Commercial banks were required to place with the central bank the ringgit funds of foreign banking institutions maintained in non-interest-bearing accounts; these funds were subsequently included in the eligible liabilities base of commercial banks.

The immediate market reaction to the 1994 measures was negative, resulting in a depreciation of the ringgit and a correction in the stock market. The controls were, however, very temporary. By the end of 1994, most of the controls were lifted. Following the onset of the Asian crisis, the ringgit came under significant pressure again in 1997. After substantial amounts of capital outflows, the authorities imposed a number of exchange and capital control measures in September 1998, aimed at containing ringgit

[3] The Malaysian experience is based on Bank Negara Malaysia Annual Report, various issues and Ariyoshi *et al*, (2000).

speculation and the outflow of capital to eliminate the offshore ringgit market and to stabilise short-term capital flows:

- The authorities closed all channels for converting ringgit funds into foreign exchange held abroad, required repatriation of foreign exchange held abroad by residents, blocked the repatriation of portfolio capital held by non-residents for 12 months, and imposed restrictions on transfers of capital by residents.

- The controls were supported by additional measures to eliminate potential loopholes (prohibiting the trading of ringgit assets offshore, announcing demonetisation of large denomination ringgit notes, and amending the Companies Act to limit dividend payments).

- The authorities replaced the policy of a managed float by pegging the ringgit to the U.S. dollar, relaxed monetary and fiscal policies to support economic activity, and accelerated financial and corporate sector reforms that had commenced in early 1998 to deal with the weak financial institutions and the banking system.

- On February 4, 1999 the authorities replaced the 12-month holding restriction on repatriation of portfolio capital with a declining scale of exit levies.

According to the Malaysian central bank, these rules were meant to encourage existing portfolio investors to take a longer view of their investments in Malaysia, attract new funds into the country, while at the same time discouraging destabilising short-term flows and penalising early withdrawals. In addition, they were designed to allow smoother outflow of funds, rather than a sudden and massive outflow upon the expiry of the one year holding period.

The Malaysian experience reflects the potential effectiveness of controls on inflows when the controls are accompanied by steps to strengthen prudential regulations and an appropriate monetary policy. The controls were effective in eliminating the offshore ringgit market, which was the locus of much of the speculative activity. In conjunction with the 12-month holding period and restrictions on resident outward investments, the suppression of the offshore ringgit market effectively constrained capital outflows.

Thailand[4]

Thailand went in for capital account liberalisation before reforming the financial sector. Capital inflows were actively promoted in Thailand since 1985 till the mid-1990s. Inflows through portfolio and equity investments were permitted freely, though portfolio and foreign direct investment outflows were subject to restrictions. Banks' foreign borrowing was unrestricted other than by net open position limits, while that by residents could be contracted freely except that proceeds needed to be repatriated to authorised banks or placed in foreign currency accounts. The Thai economy started showing signs of overheating in mid-1993. The liberalisation of short-term flows, combined with high domestic interest rates and an implicit exchange rate guarantee, led to a substantial and unsustainable build-up of short-term liabilities by banks and non-banks during early 1995.

Not willing to give up the fixed exchange rate regime, the authorities attempted to cope with capital inflows through a combination of monetary, prudential and market-based capital control measures. The policy rate was raised in March 1995. Sterilisation measures were stepped up. In addition, some measures designed to target capital flows more directly were introduced in August 1995:

- Asymmetric open position limits for short and long positions (with smaller limits on short foreign currency positions in an attempt to discourage foreign borrowing abroad);
- Reporting requirement for banks on risk control measures in foreign exchange and derivatives trading; and
- A seven per cent reserve requirement (held at the central bank) on non-resident baht accounts with less than one-year maturity and on finance companies' short-term foreign borrowing.

The persistent growth in net total and short-term capital inflows in 1995 prompted the authorities to introduce a second round of measures in April-June 1996. The seven per cent reserve requirement was extended to non-resident baht borrowing with a maturity of less than one year and to new short-term offshore borrowing of maturities of less than one year by commercial banks.

[4] The Thai experience has been drawn mainly from Ariyoshi *et al* (2000) and Johnston *et al*, (1997).

The Thai baht came under speculative pressure by mid-1997. To stabilise the foreign exchange market and stem speculative attacks on the baht, the authorities imposed a series of measures to limit capital outflows in June 1997:

- Financial institutions were asked to refrain from, and then suspend (June 1997), transactions with non-residents that could facilitate a build-up of baht positions in the offshore market (including baht lending through swaps, outright forward transactions in baht, and sales of baht against foreign currencies).
- Any purchase before maturity of baht-denominated bills of exchange and other debt instruments required payment in U.S. dollars.
- Foreign equity investors were prohibited from repatriating funds in baht (but were free to repatriate funds in foreign currencies).

These measures gave rise to a two-tier currency market, with separate exchange rates for investors who bought baht in domestic and overseas markets. With the persistent expectations of baht devaluation driving capital outflows, foreign exchange reserves remained under pressure and the authorities eventually abandoned their pegged exchange rate regime and floated the baht on July 2, 1997.

Thailand's capital controls provided temporary relief. Circumvention was facilitated because of presence of offshore market with arbitrage opportunities. Re-imposition of controls along with weak economic fundamentals undermined investor confidence and reduced inflows. Once the economic situation showed signs of improvement and the Bank of Thailand lifted controls in 1998 unifying the two-tier market, baht appreciated and stock prices improved.

South Korea

Over the course of the late 1980s, South Korea pursued a policy of gradually liberalising the domestic financial system and the capital account, although this was accelerated in 1993. In 1988, South Korea accepted Article VIII obligations ensuring full convertibility for current account transactions. In the early 1980s, capital inflows were liberalised and capital outflows restricted to assist the financing of current account deficits. Later in the decade, when Korea began to run substantial current account surpluses, controls were reimposed on inflows and controls on outflows were eased. This position was reversed in early 1990s as a consequence of the strong won. Liberalisation of the capital account was gradual and selective and a comprehensive liberalisation plan was not adopted until 1993. Policy thereafter was oriented towards gradually liberalising capital account transactions. Korea's policy towards capital account transactions was, thus, guided by developments in the current account. Financial sector reform, including efforts to improve regulation and supervision, was pursued concurrently (Coe and Se-jik, 2002 and IEO, 2003).

As part of the reform process, Korea moved from pegging the won to a basket of currencies to the Market Average Exchange Rate (MAER) system in order to allow exchange rates to be determined more by market forces. One key consequence of the increased access of Korean financial institutions to external financing was a rapid expansion of foreign debt, which nearly trebled from $ 44 billion in 1993 to $120 billion in September 1997. While this level of foreign debt accounted for only 25 per cent of GDP in 1997, which was considerably lower than that of other comparable countries, a critical dimension was the maturity structure of the debt. The share of short-term debt rose from an already high 43.7 per cent in 1993 to an extremely high 58.3 per cent at the end of 1996. Newly-licensed merchant banks, most of them owned by *chaebols* assumed a very large share of this short-term debt. The policy of liberalising short-term flows before long-term flows and restricting direct raising of capital by non-financial firms gave the merchant banks a profitable niche. The merchant banks were required to keep their currency exposures in balance, but there were many loopholes in these rules and supervision was poor. Thus, although measures were undertaken in the 1990s to liberalise and strengthen the financial sector, persistent weaknesses of oversight and regulation remained.

Korea was hit by the Asian financial crisis of 1997 as the sharp rise in the short-term debt to reserves ratio and concerns about the stability of the financial sector (especially the finance companies) encouraged continual pressure against the won. When the won was forced out of its trading band, its value collapsed.

Korea adopted financial and corporate restructuring policies following the crisis and recovered fast, and is currently showing robust growth rates. In recent years, Korean won was allowed to appreciate but at the same time, the country attempted to maintain export competitiveness of the country. While currency value is allowed to be determined by market fundamentals, interventions ensure smoothing of the currency path.

Experience of other EMEs

Russia

Russia started slowly liberalising its capital account in the early 1990s, but in 1998, Russia faced a serious currency crisis due to its fiscal situation. In August 1998, Russia introduced a series of emergency measures, including re-intensification of capital controls and the announcement of a debt moratorium. The unilateral debt restructuring and moratorium was reflected in a downgrading of sovereign credit ratings in early 1999 and a complete halt in access to international capital markets. FDI declined sharply. The exchange rate band was abandoned and the currency depreciated sharply. Russia recovered with the help of subsequent reforms and has recorded an average growth of 7 per cent in the last three years. Russia lifted the last remaining capital restrictions effective July 1, 2006 clearing the way for making the currency fully convertible. Such restrictions included a 7.5 per cent mandatory reserve requirement for non-resident holders of sovereign debt. They also involved an obligation to hold proceeds from the sale of sovereign debt temporarily in a special rouble account before converting the roubles into foreign currency. Earlier in the year, the central bank abolished the compulsory sale of 10 per cent of foreign earnings by Russian entities. Foreigners were also permitted better access to the Russian bond market. The move to full capital account convertibility is expected to make the domestic Russian debt market more attractive to foreign investors, but little immediate impact is expected on the rouble's exchange rate that is currently linked to a bi-currency basket. It is estimated that Russia has the second largest amount of dollar bills in circulation after the US. With convertibility, Russians who keep their savings in US dollar are likely to opt for rouble, speeding up 'de-dollarisation' of the country's economy (Humber, 2006 and Mosnews, 2006).

Brazil

Brazil was impacted by both the East Asian and the Russian crisis and was taking steps to avert its intensity when inflows of private foreign capital suddenly dried up. At the time of financial crisis in 1999, Brazil suffered from both fiscal and balance of payments weaknesses: in mid-1998, the bulk of the government's domestic debt - which amounted to 40 per cent of GDP - consisted of short-term financing. The current account deficit was approaching 5 per cent of GDP. In August 1998, capital flows to Brazil came to a halt. These events forced Brazil to float the *real* which led to a sharp depreciation in February 1999 and threatened to fuel inflation while driving the economy into a deep recession. The *real* was allowed to continue to float and Brazil adopted inflation targeting in two steps to enhance the credibility of its macro-economy. Interest rates were as high as 39 per cent and had to be raised further, given the inflationary potential due to sharp depreciation. Subsequently, a remarkable turnaround in the fiscal situation to a surplus helped Brazil in resolving the crisis as the debt-to-GDP ratio stabilised. The central bank started the practice of lowering rates between meetings of the MPC which reduced the inflationary expectations. This measure, coupled with greater information disclosure, helped in stabilising international financial flows and the exchange rate and the interest rate. Dependence on short-term credit (other than trade finance) to finance the balance of payments was reduced and maturities of the government's domestic debt were lengthened. Brazil was broadly able to adhere to the announced inflation targets and witnessed a return to growth thereafter (Fraga, 2000 and IEO, 2003).

Argentina

In the mid-1990s, Argentina displayed strong economic performance: the hyperinflation of the 1980s came down to low single digits, output growth was impressive, and the economy had successfully weathered the Mexican crisis of the mid-1990s. The current and capital account transactions were both liberalised simultaneously in 1991, and Argentina embarked on a currency board arrangement pegged to US dollar from April 1991. Major weaknesses however, emerged during the boom years of the 1990s, including the build-up of public debt and the failure to tackle serious structural weaknesses in fiscal institutions, labour markets, and external trade. These weaknesses came into play with the onset of a prolonged depression beginning in mid-1998 on account of several factors: cyclical correction, domestic political uncertainties, financial contagion from the 1998 Russian crisis, and Brazil's 1999 crisis and the subsequent devaluation of Brazil's currency. Once the downturn had started, the currency board arrangement limited the Argentine authorities' ability to manage macroeconomic policies in a counter-cyclical manner. In 2001-02, Argentina experienced one of the worst economic crises in its history. Output fell by about 20 per cent over three years, inflation came back, the government defaulted on its debt, the banking system was largely paralysed, and the Argentine *peso* depreciated sharply. When the economy slid into recession, the currency board became a liability in the context of a build-up of sizable foreign currency-denominated public debt. The currency board was abandoned in January 2002, and the *peso* was first devalued and later floated, thereby totally backtracking from the hard peg combined with re-imposition of several current and capital account restrictions. In the early months of 2003, the economy began to recover and in 2005, after three years of around 9 per cent growth, real GDP has surpassed its 1998 peak by some 6 per cent, led by strong investment and consumption. The economy has benefited from a favourable terms of trade, significant reduction in the debt burden following the 2005 debt restructuring, and a competitive currency. However, inflation after touching a low of 3 per cent in 2003 has risen steadily to 12.3 per cent in 2005. The external accounts have improved remarkably aided by favourable global commodity prices and the emergence of Asia as a key export destination which have increased earnings from primary and agro-industrial exports. At the same time, net private capital flows turned positive in 2005 for the first time since 1999. In a nutshell, the adverse interaction between currency board arrangement and fiscal dynamics played the central role in Argentine crisis of 2001-02, combined with adverse external developments (Daseking *et al*, 2004; IMF, 2006)

Turkey

Huge requirements for public sector borrowing in 1993 and early 1994, combined with major policy errors in financing the deficit, led to Turkey's currency crisis in 1994. As a result, output fell by 6 per cent, inflation rose to three-digit levels, the central bank lost half of its reserves, and the exchange rate (against the U.S. dollar) depreciated by more than half in the first three months of the year. Again, Turkey faced a serious currency crisis during November-December 2000 when the overnight inter-bank interest rates climbed as high as 1700 per cent while domestic interest rates reached 60 per cent and fearing an impending liquidity crisis, foreign investors immediately took their money out from Turkey. This was followed by another crisis which began on February 19, 2001 due to domestic political dissensions and the foreign investors and creditors started panic buying of Euro to cover their exposure from impending economic and political crisis. There has been a sharp decline of the Turkish lira over the past few months due to a massive sale of Turkish assets by international investors - as in other emerging markets - due to external factors, including the tightening of monetary policy in the United States, the euro zone and Japan coupled with the domestic political uncertainty caused by the forthcoming elections, a large government debt, a growing current account deficit and dependence on short-term capital inflows (Celasun, 1998; Bibbee, 2001).

Chile

Chile faced a surge in private capital inflows beginning 1989. With monetary policy adhering to a domestic inflation target and exchange rate geared towards achieving an external current account target, complete deregulation of capital flows resulted in a classical monetary policy dilemma. The initial policy response was sterilised foreign exchange intervention and a tightening of fiscal policy. With sterilisation costs becoming sizable, the authorities in June 1991 introduced selective controls on capital inflows (Schneider, 2000):

- A 20 per cent unremunerated reserve requirement (URR) on foreign borrowing. The URR, an indirect/price-based capital control, was designed to indirectly tax short-term capital inflows (a form of Tobin tax). Initially, the URR covered foreign loans (except for trade credit), but over time its coverage was extended to non-debt flows that had become a channel for short-term portfolio inflows (i.e., foreign currency deposits in commercial banks, and even foreign direct investments of a potentially speculative nature). The rate of the URR was raised from 20 per cent to 30 per cent, until a decline in capital inflows, reflecting contagion from the Asian crisis, motivated a reduction of the rate. In September 1998, the URR was suspended by reducing its rate to zero per cent.

- The URR was also supported by restrictive measures such as a minimum stay requirement for direct and portfolio investments from abroad; some regulatory requirements for domestic corporations borrowing abroad; and extensive reporting requirements on banks for capital transactions.

Along with these controls, supporting measures such as liberalisation of capital outflows started in the early 1990s which was expected to relieve the pressure on net capital flows.

The use of capital controls in Chile has been part of a broad program of economic reforms involving a coherent set of macroeconomic and structural policies implemented throughout the 1990s. Chile depicts a successful experience in CAL using judicious controls along with liberalisation and economic reforms. Chile could well recognise the significance of financial reforms (in establishing a sound prudential framework and a strong credit culture) for the success of economic reforms[5] .

China

China has been following a policy of gradualist economic reforms since late 1978. A closed economic system was rapidly opened to trade and investment. China allowed yuan to be freely convertible under current account in December 1996. There are, however, extensive restrictions on inflows and outflows of money for capital account transactions (BIS, 2003).

On July 21, 2005 China abandoned its eight-year peg to the dollar and moved to a managed floating exchange rate regime. Since then, the renminbi (RMB) has appreciated, *albeit* marginally. China continues to take steps to create market infrastructure and financial instruments for a floating currency. They introduced an inter-bank foreign currency trading system in early 2005. They also introduced new financial products to hedge against currency appreciation such as forwards. China has taken

[5] At present, Chile has controls on derivatives and commercial credits. There are provisions specific to commercial banks and other credit institutions and institutional investors.

steps to liberalise controls on capital movements to increase the depth and liquidity in foreign exchange markets. It has continued to expand the program that allows FIIs to buy shares in locally listed companies. Chinese residents and institutional investors have also been increasingly allowed to acquire overseas assets. But, China still maintains extensive controls on outflow of capital than it does on inflows. The country remains reticent to open capital account partly due to its weak financial system and the need to substantially strengthen regulations and prudential supervision. The authorities have recently announced that China will push ahead with yuan convertibility 'step by step'. 'Yuan convertibility' is a systematic project and has to accommodate the nation's macroeconomic and financial reform. The Chinese government realises that capital account liberalisation is in the country's best long-term interests and moving in this direction is inevitable. In the last few years, China has announced the following liberalisation measures on capital flows.

2003

- Chinese authorities introduce measures that promote FDI and other capital flows.
- Qualified Foreign Institutional Investor (QFII) program launched. (QFII: Qualified Foreign Institutional Investor – a foreign entity allowed to invest upto a certain quota amount in China's domestic capital markets).

2004

- July-August: Select Chinese domestic institutional investors (ADII) authorised to invest in overseas assets.
- November/December: Limits raised on amounts emigrants, travellers, and students can take out of China.

2005

- February: Eliminated surrender requirements on certain commercial firms' forex receipts.
- June: Raised quota for QFIIs from $ 4 billion to $ 10 billion.

2006

- April: Liberalised forex regulations allowing Chinese firms/residents to buy more foreign assets. (April 2006: Individuals can convert more RMB to take out of China, commercial banks can buy foreign bonds; securities firms can buy foreign assets).

- April: 54 foreign and domestic banks operating in China allowed to trade forex swaps.

China also had record current account surplus and its official external debt was modest. The focus on attracting certain forms of FDI on an integrated, geographically-targeted basis, and gradual opening up of financial sector has also helped in attracting stable capital inflows into China.

China has committed to open the external sector to foreign investment as part of WTO accession with substantive liberalisation to be completed by 2007 (Lu, 2006). This looming deadline has forced Chinese government to accelerate steps to strengthen reforms in the banking system.

Section IV

Extant Capital Account Restrictions

The 2005 *Annual Report on Exchange Arrangements and Exchange Restrictions* records that the changes in exchange rate regimes indicated a move towards more flexible regimes by several countries and the general thrust of changes affecting the regulatory framework of foreign exchange transactions was towards the easing of controls including capital account transactions. Changes in the prudential measures of many countries were also directed towards the easing of requirements. The category in which several countries appear to have become restrictive pertains to the regulation of the inflow of foreign direct investments. However, the limitations in this category are often motivated by reasons other than economic factors – similar to the regulation of real estate investments by non-residents. Of late, however, there has been a significant increase in notifications to the IMF involving the enforcement of restrictions for security reasons. These restrictions were introduced consequent to the emphasis on preventing the financing of terrorism.

Based on the reporting by member countries, the IMF report for 2005 shows that only 16 countries do not have restrictions on payment for capital transactions (Italy, Spain, Luxemburg, Israel and Hong Kong among the advanced countries and Gambia, Zambia, Kiribati, Iraq, Bolivia, Guatemala, Haiti, Nicaragua, Panama, Peru and Uruguay among the EMEs and developing countries).

Though, the Article 56 (1) of the EC Treaty holds that 'all restrictions on the movement of capital between Member States and between Member States and third countries' stand prohibited, Articles 57 to 60 of the Treaty provide for certain qualifying restrictions which would not be construed as violation or arbitrary discrimination or disguised restriction on the free movement of capital and payments. These qualifying restrictions are summarised below:

Article No.	**Qualifying restrictions**
57	Restrictions which exist on 31st December 1993 under national or community law adopted in respect of movement of capital involving direct investment - including in real estate - establishment, the provision of financial services or the admission of securities to capital markets.
58(1)(a)	Application of tax law distinguishing between taxpayers on the basis of residence or with regard to the place where the capital is invested.
58(1)(b)	Requisite measures to prevent infringements of national law in the fields of taxation, prudential supervision of financial institutions, lay down procedures for statistical information or measures on the grounds of public policy and public security.
58(2)	Restrictions on the right of establishment.
59	In exceptional circumstances, movement of capital to or from third countries cause, or threaten to cause, serious difficulties for the operation of economic and monetary union (by qualified majority, the Council after consulting ECB, may take safeguard measures with regard to third countries for a period not exceeding six months, if such measures are strictly necessary).
60(1)	For serious political reasons and on grounds of urgency in the light of common foreign and security policy, Member States may take unilateral measures with regard to capital movement and payments.
60(2)	In the event of serious internal disturbances affecting law and order or in the event of war to take urgent measures on the movement of capital and payments.

Source: Courtesy - Shri U.S. Das, IMF, Washington

Thus, most countries are observed to retain a variety of capital controls with specific provisions relating to banks and credit institutions and institutional investors. The position is summarised in Table 4 below.

Table 4: Summary of Features of Controls on Capital Transactions in IMF Member Countries

(Total number of countries: 184)

Features of Controls on Capital Transactions	Total no. of
Countries with this feature	
1. Capital Market Securities	126
2. Money Market Transactions	103
3. Collective Investment Securities	97
4. Derivatives and Other Instruments	83
5. Commercial Credits	98
6. Financial Credits	109
7. Guarantees, Sureties and Financial backup Facilities	87
8. Direct Investment	143
9. Liquidation of Direct Investment	54
10. Real Estate Transactions	135
11. Personal Capital Transactions	97
Provisions specific to	
(a) Commercial banks and Other Credit Institutions	157
(b) Institutional investors	91

Note: India figures under all these items.

Source: IMF, *Annual Report on Exchange Arrangements and Exchange Restrictions, 2005*

Section V

Lessons from Country Experiences

The experience of the countries recounted above with respect to capital account liberalisation and lessons drawn therefrom are summarised below:

- Liberalisation of the capital account was gradual in most of the advanced economies in the run up to full convertibility, combined with strengthened financial systems and prudential regulations. Even after "fully" liberalising the capital account these countries continue to maintain certain capital controls.

- Experience of some of the Asian and Latin American economies, which liberalised their capital account in the 1980s and later backtracked by imposing controls, shows that even after full capital account convertibility, there is a need for safety valves in the form of regulatory safeguards to meet potential capital account crises.
- Gradual liberalisation should not be used as a shield for weak economic policies by continuing to retain several controls. Instead, gradual liberalisation should be used as a tool for furtherance of sound macroeconomic and prudential policies prior to full CAL (France).
- Gradual process of CAL does not eliminate the risks of crisis or pressures in the foreign exchange market (France, Japan). These risks, however, get minimised when an integrated approach to reform is taken involving macroeconomic stabilisation and institutional strengthening.
- Along with other reform measures, exchange rate flexibility is important while undertaking CAL. Fixed exchange rate regime reduces the incentive to hedge foreign currency borrowing. Floating exchange rates reduce such incentives. Under a flexible exchange rate scenario, monetary policy flexibility can be a useful tool to help maintain macro-economic stability.
- Capital controls could temporarily relieve the pressures on the balance of payments but they cannot provide lasting protection when the fundamental causes of the imbalances remain unaddressed.
- Partial system of capital control that seeks to discriminate between types of flows or destinations provides incentives for circumvention and is vulnerable to diversion of capital flows to unregulated financial markets.
- Limiting fiscal imbalances and preventing excessive build-up of domestic debt is essential to avoid chances of backtracking subsequent to CAL. Though fiscal consolidation may not by itself be a sufficient condition to prevent crises, it has been a necessary component of liberalisation and its absence can lead to instability (Brazil).
- Emerging market economies have managed heavy inflows subsequent to liberalisation through sterilisation, though later most of them have

reimposed capital controls faced with the limitations of sterilisation.

- Avoiding real exchange rate misalignment could minimise effects of crisis. This also gives room for pursuing autonomous monetary policy. It would force market participants to hedge their positions which would be beneficial for forex market development. Most of the developing countries have opted for greater flexibility in their exchange rate regimes as CAL has progressed.

- Given the increased risks that are prevalent in a deregulated environment, it is important to focus on effective risk management strategies, improve prudential supervision and develop proper reporting standards to meet the emerging challenges.

Most of the advanced economies used capital controls extensively during the phase of run up to full convertibility. Once these economies went in for CAL in the late 1970s and 1980s, cases of reintroduction of controls were rare. The financial environment in which countries operate today has however changed dramatically from the 1960s and 1970s when the advanced countries were able to use controls. Liberalisation and deregulation, combined with advancement of information and communications technology, has increased the complexity and sophistication of the global financial markets. The range of financial instruments being used by market participants has increased. Financial markets react swiftly to new information and changed circumstances and also exhibit higher risks and volatility. Under such circumstances, use of controls for a prolonged period may not be very effective. At the same time, rapid easing of capital controls and subsequent backtracking seen in the case of many Asian and Latin American countries, clearly indicate the need for a more cautious and calibrated approach, and ensuring enough regulatory and prudential safeguards before moving towards capital account liberalisation, if risks of substantial backtracking are to be minimised.

Annex 1

Chronology of Key Changes in Capital Account Controls in Select Advanced Countries

1. United States

1963 July	T Announcement of introduction of Interest Equalisation Tax (enacted 1964).
1965 March	T Introduction of voluntary guidelines limiting foreign lending and investment.
1968 January	T Guidelines limiting foreign direct investment made mandatory.
1974 January	L Abolition of capital controls, including voluntary guidelines.
	2. Japan
1960 June	L Controls on foreign direct investment eased.
July	L Introduction of non-resident free yen accounts.
1967 July	L Further easing in foreign direct investment regulations.
1971 July	L Restrictions on outward direct and portfolio investment eased.
September	T Restrictions on yen conversion of advance export receipts.
1972 June	T Marginal reserve requirement imposed on non-resident free yen accounts.
October	T Restrictions on the purchase of Japanese securities by non-residents.
November	L Restrictions on portfolio outflows eased further.
1973 November	L Easing of restrictions on the advance receipt export payments.
November	T Acquisition of foreign short-term (maturity less than 6 months) securities by residents restricted.
December	L Easing of restrictions on the purchase of Japanese securities and lowering of the marginal reserve requirement of non-resident free yen accounts.
1974 January	T Tightening of portfolio outflow restrictions, including voluntary restraints on institutional investors.
April	T Japanese banks instructed to no finance “non-urgent” foreign direct investment.
September	L Marginal reserve requirement on non-resident free yen accounts abolished.

1977 March	L Abolition of “voluntary restraints” on banks’ purchase of foreign securities.
June	L Restrictions on foreign currency accounts of residents eased.
June	T Reserve requirements introduced on foreign currency liabilities of foreign exchange banks, residents’ external foreign currency deposits and non-resident free yen accounts.
1978 March	T Marginal reserve requirement on non-resident free yen accounts increased, further restrictions on portfolio inflows.
1979 February	L Marginal reserve requirement on non-resident free yen accounts abolished.
February	L Restrictions on non-resident purchase of bonds eased.
May	L Easing of restrictions on portfolio flows.
1980 March	L Easing of restrictions on portfolio inflows.
December	L Revision of the Foreign Exchange and Foreign Trade Control Law.
1983 April	L Abolition of requirement to link forward exchange transactions to trade.
May	L Publication of the “Report on yen/dollar exchange issues”.
June	L Further easing of portfolio flows.
June	L Liberalisation of short-term euro/yen lending by Japanese banks.
1985 May	L Abolition of prior notification requirement for residents borrowing short-term euro/yen.
1986 August	L Easing of limits on off-shore investment by institutional investors.
December	L Japanese Off-shore Market (JOM) opened.
1989 April	L Easing in restrictions on flows of funds between JOM and domestic markets.
1991 April	L Restrictions on inward foreign direct investment eased.
1998 April	L Introduction of new Foreign Exchange and Foreign Trade Control Law.
	3. Australia
1972 September	T Short-term overseas borrowing restricted.
December	T Those undertaking long-term overseas borrowing required to hold a non-interest bearing deposit with the Reserve Bank.

1973 March	T Restrictions on inward investment in real estate imposed.
1977 July	L Requirement to hold a non-interest bearing deposit with the Reserve Bank when borrowing overseas suspended (and not reintroduced).
1981 July	L Monetary limits on overseas investment in equity or real estate abolished.
1983 December	L Restrictions on interest-bearing investments by non-residents abolished.
December	L The exchange rate was floated.
1985 January	L A range of portfolio controls abolished.
October	L Restrictions on inward direct investment eased.
1992 February	L Restrictions on inward direct investment eased further.
	4. Italy
1972 June	T Introduction of measures aimed at restricting capital outflows; ban on net external credit position of banks; suspension of external convertibility of Italian banknotes.
1973 January	T Establishment of a dual exchange market.
July	T Introduction of a 50 per cent compulsory non-interest bearing deposit scheme with respect to most capital outflows.
1974 March	L Abolition of the dual exchange market.
May	T Introduction of a temporary compulsory non-interest bearing deposit scheme with respect to imports, excluding raw materials, oil and investment goods. Italy is authorised by the Commission to invoke safeguard measures.
1976 March	T Reintroduction of compulsory bank financing in foreign exchange for advance settlement of imports.
May	T Reintroduction of the non-interest bearing import deposit scheme.
October	T Imposition of a temporary special tax on purchases of foreign currency and payments abroad. Extension of the compulsory import deposit scheme.
1977 February	L Expiration of the special tax on foreign currency purchases.
April	L Abolition of the compulsory import deposit scheme.
1981 May	T Reintroduction of the non-interest-bearing deposit scheme with respect to purchases of foreign currency by residents.

1982 February	L Abolition of the advance deposit scheme.
1983 December	L Certain direct investment abroad is exempted from the 50 per cent non-interest-bearing deposit requirements.
1984 December	L Reduction of compulsory zero-deposit requirements on portfolio investment abroad.
1985 October	L Abolition of the compulsory deposit requirement for direct investment abroad. Residents' foreign exchange deposits are freely convertible into other currencies and the ban on transfer of foreign securities and loans between residents is lifted. Reduction of compulsory deposit requirements on other transactions.
1986 August	L Restoration of external convertibility of Italian banknotes.
1987 March	T Introduction of reserve requirement on bank deposits in foreign currency.
May	L Abolition of the non-interest-bearing deposit requirement for investment abroad in securities and real estate.
September	T Shortening of holding periods of foreign currencies.
1988 June	L Restrictions on tourist spending are eased.
October	L Introduction of a positive system of exchange control. Significant relaxation of controls.
1990 January	L Abolition of restrictions on purchases of foreign securities by residents.
May	L Abolition of all remaining exchange control regulations.

T: Tightening of controls; L: Loosening of controls

Source: Bakker and Chapple (2002).

Annex-2

CONTROLS ON CAPITAL ACCOUNT TRANSACTIONS

Feature	**Extant Capital Restrictions**
United States	
On capital market securities Shares or other securities of a participating nature	*Purchase locally by non-residents* – Laws on inward direct investment apply to purchases in the United States by non-residents of securities. There are also some restrictions specific to state legislative jurisdiction in the banking, securities, and insurance sectors.
	Sale or issue locally by non-residents – Public offers in the United States or to U.S. residents by foreign investment companies are prohibited.
On Money market instruments	*Sale or issue locally by non-residents* – Foreign mutual funds are restricted.
On collective investment securities	*Sale or issue locally by non-residents* – The regulations governing shares and other securities of a participating nature apply.
Controls on credit operations	*Financial Credits – by residents to non-residents* – The Johnson Act prohibits, with certain exceptions, persons within the United States from dealing in financial obligations or extending loans to foreign governments (other than IMF/World Bank members) that have defaulted.
Controls on direct investment	*Outward direct investment* – Controls for security reasons to certain countries.

Note: Compiled from *Annual Report on Exchange Arrangements and Exchange Restrictions*, IMF, 2005.

Feature	Extant Capital Restrictions
Inward direct investment	Laws on inward direct investment apply to purchases in the United States by non-residents. Also, controls on investment transactions for security reasons from some countries.
Controls on real estate transactions	*Purchase locally by non-residents* – Ownership of agricultural land by foreign nationals or by corporations in which foreign owners have an interest of at least 10 per cent or substantial control must be reported to the Department of Agriculture. Certain states in the United States impose various controls on foreign nationals' purchases of land within their borders.
Provisions specific to commercial banks and other credit institutions	*Investment regulations* – Banks are subject to prudential oversight in these areas.
	Open foreign exchange position limits – Banks are subject to prudential oversight and reporting requirements.
China	
On capital market securities Shares or other securities of a participating nature	*Purchase locally by non-residents* – Qualified foreign institutional investors (QFIIs) may invest domestically in A shares, subject to certain limitations. B shares denominated in U.S. dollars or Hong Kong dollars and are listed on the Chinese Securities Exchange may be bought by foreign and domestic investors. Domestic investors may purchase B shares with new or existing foreign currency deposits.
	Sale or issue locally by non-residents – These transactions are limited to B shares. Foreign institutional investors, however, can invest in treasury bonds, convertible bonds, and corporate bonds listed on domestic security exchanges.

Feature	**Extant Capital Restrictions**
	Purchase abroad by residents – Overseas listed domestic companies may repurchase the shares issued by them provided that the SAFE verifies the source of the fund and approves payment abroad.
	Sale or issue abroad by residents – restricted.
Bonds or other debt securities	*Sale or issue locally by non-residents* – These transactions are not permitted.
	Purchase abroad by residents – Banks authorised by the China Banking Regulatory Commission (CBRC) and insurance companies authorised by the China Regulatory Commission and the SAFE may purchase foreign bonds.
	Sale or issue abroad by residents – Following authorisation. Foreign exchange earnings from bond floatation must be repatriated.
On money market instruments	*Purchase locally by non-residents* – Non-residents are not allowed to purchase money market instruments.
	Sale or issue locally by non-residents – Non-residents are not allowed to sell or issue money market instruments.
	Purchase abroad by residents – The regulations governing bonds or other debt securities apply.
	Sale or issue abroad by residents – These transactions are subject to SAFE approval.

Feature	Extant Capital Restrictions
On collective investment securities	*Purchase locally by non-residents* – Qualified foreign institutional investors may invest in domestic closed-end and open-end funds.
	Sale or issue locally by non-residents – These transactions are not allowed.
	Purchase abroad by residents – The regulations governing purchases of money market instruments apply.
	Sale or issue abroad by residents – The regulations governing the sale or issue of money market instruments apply.
Controls on derivatives and other Instruments	*Purchase locally by non-residents* – These transactions are not allowed.
	Purchase locally by non-residents – These transactions are not allowed.
	Sale or issue locally by non-residents – These transactions are not allowed.
	Purchase abroad by residents – Only financial institutions that are approved by the CBRC and carry out foreign exchange trading operations for their own account or on behalf of customers may purchase without SAFE approval, both transactions are subject to SAFE approval and restrictions.
Controls on credit operations	Purchases of foreign exchange for advance repayment of foreign debt require SAFE authorisation.

Feature	**Extant Capital Restrictions**
Commercial credits	*By residents to non-residents* – Financial institutions authorised by the CBRC may lend to overseas institutions or contract overseas credits.
	To residents from non-residents – Medium – and long-term international commercial borrowing by Chinese institutions must be incorporated in the state plan for the use of foreign capital and undergo transaction based examination.
	FFEs may borrow from non-residents without obtaining prior approval but must register the borrowing with the SAFE.
	Financial credits – The regulations governing commercial credits apply.
	By residents to non-residents: Restricted.
	To residents from non-residents: Restricted.
Guarantees, sureties, and financial backup facilities	*By residents to non-residents* – Financing guarantees provided by domestic Chinese banks and other domestic institutions (with the exception of wholly foreign-owned enterprises) require prior SAFE approval.
	To residents from non-residents – Domestic institutions may accept guarantees from foreign institutions.
Controls on direct investment	A three-tier classification system is in effect, defining activities in which foreign exchange investment is encouraged, restricted, or banned.

Feature	**Extant Capital Restrictions**
Outward direct investment	Outward direct investment is permitted only after examination of the source of the foreign exchange funds and approval of the authorities concerned. In some provinces and regions, the limit on outward investment is the equivalent of US $ 3 million.
Inward direct investment	Non-residents are free to invest in China as long as they meet requirements under Sino foreign joint-venture laws and other relevant regulations, and are approved by the Ministry of Commerce. For environmental and security reasons, inward direct investment in some industries is prohibited.
Controls on liquidation of direct Investment	Prior approval is required.
Controls on real estate transactions	The regulations governing direct investment apply.
Purchase abroad by residents	Restricted.
Purchase locally by non-residents	Restricted.
	Sale locally by non-residents – With SAFE approval.
Controls on personal capital Transactions Loans	*By residents to non-residents:* Restricted.
	To residents from non-residents: Restricted.

Feature	Extant Capital Restrictions
Gifts, endowments, inheritances, and Legacies	*By residents to non-residents* – Restricted and subject to complex procedures.
	To residents from non-residents – Restricted and subject to complex procedures.
Transfer of assets	*Transfer abroad by emigrants* – Routine foreign exchange revenues, including retirement and pension funds, may be remitted abroad.
Provisions specific to commercial Banks and other credit institutions	The limits and restrictions are set by the Monetary Authority for prudential reasons.
	Borrowing abroad – The regulations governing commercial credits apply. Effective June 27, 2004, domestic banks that are foreign funded may not convert proceeds from debt contracted abroad into renminbi and are not allowed to purchase foreign exchange to service these debts.
	Maintenance of accounts abroad – Registration with the SAFE is required for domestic banks to open foreign exchange accounts abroad. Domestic nonbank financial institutions and nonfinancial enterprises require prior approval by the SAFE.
	Lending to non-residents (financial or commercial credits) – The regulations governing commercial credits apply.
	Lending locally in foreign exchange – Lending is subject mainly to review of qualifications by the PBC and to asset–liability ratio requirements.
	Purchase of locally issued securities denominated in foreign exchange: Securities denominated in foreign currency are not currently issued.

Feature	Extant Capital Restrictions
Differential treatment of deposit accounts in foreign exchange	*Liquid asset requirements* – The ratio of all liquid foreign exchange capital to all liquid foreign exchange liabilities may not be less than 60%.
	Credit controls – The ratio of the credit balance for a single borrower to a bank's net capital may not exceed 10%.
	Investment regulations – Bank equity investment should not exceed the difference between bank capital and mandatory paid–in capital. Nonbank financial institutions' total equity investment (excluding trust accounts) should not exceed the difference between their capital and mandatory paid-in capital.
	Abroad by banks – Investment in foreign securities other than equities on foreign securities markets by banks is subject to quarterly approval by the PBC.
	In banks by non-residents – PBC approval is required.
	Open foreign exchange position limits – For financial institutions trading foreign exchange on their own behalf, the daily total amount traded (total open foreign exchange position) should not exceed 20% of the foreign exchange working capital. As authorised by the highest level of management, financial institutions trading foreign exchange on their own behalf may retain a small amount of overnight open position, but this should not exceed 1% of the foreign exchange working capital or foreign exchange operating funds.
	On resident assets and liabilities : Restricted.
	On non-resident assets and liabilities : Restricted.

Feature	Extant Capital Restrictions
Argentina	
Controls on capital transactions	Inward and outward foreign exchange transactions must be registered. Foreign exchange that enters the domestic market may be transferred out 365 days after its entry, except in the case of foreign trade operations and direct investment.
	New financing in the form of financial credits to or bond issues by private borrowers must be matched by foreign exchange sales to the MULC.
	The prior approval requirement for servicing nonfinancial and financial private debt is applicable only for debts of financial institutions that have opted for the BCRA's refinancing mechanism (matching).
	Monthly ceiling for purchases of foreign exchange by residents for various transactions, across all financial institutions apply.
	Also, a monthly cap is applied on purchases of foreign exchange by non-residents for various transactions.
Controls on capital and money Market instruments	Non-resident portfolio investors are required to deposit 30% of their investment in an unremunerated account for one year.
On capital market securities Shares or other securities of a Participating nature	*Sale or issue locally by non-residents* – Under the regulations of the National Securities Commission (CNV), foreign and Argentine issuers must meet the same requirements to make a public offering of securities in Argentina.

Feature	Extant Capital Restrictions
	Purchase abroad by residents – Although there are no specific controls on residents' purchases of foreign securities abroad, their purchases may be limited as a result of restrictions on capital flows from Argentina to foreign jurisdictions.
Bonds or other debt securities	*Sale or issue locally by non-residents* – The regulations governing the sale or issue of shares or other securities of a participating nature apply.
	Purchase abroad by residents : Restricted.
	Sale or issue abroad by residents : Restricted.
On money market instruments	The regulations governing the foreign exchange aspects of bonds or other debt securities apply.
	Purchase locally by non-residents : Restricted.
	Sale or issue locally by non-residents – The regulations governing domestic issuers also apply.
	Purchase abroad by residents – The regulations governing bonds or other debt securities apply.
	Sale or issue abroad by residents : Restricted.
On collective investment securities	*Purchase locally by non-residents* : Restricted.
	Sale or issue locally by non-residents – Approval by the CNV is required for public offerings.

Feature	Extant Capital Restrictions
	Purchase abroad by residents – The regulations governing bonds or other debt securities apply.
	Sale or issue abroad by resident: Restricted.
Controls on derivatives and other Instruments	Without approval by the BCRA, authorised foreign exchange dealers may engage in arbitrage and swaps only with foreign banks or holding companies located in a Bank for International Settlements member state and that have at least an A rating from one of the rating agencies registered with the BCRA, or with institutions owned by foreign governments. (Subject to complex procedures).
	Purchase locally by non-residents: Restricted.
	Sale or issue locally by non-residents: Approval by the CNV is required for public offerings.
	Purchase abroad by residents – Access to the foreign exchange market for forward and other derivatives contracts – except for currency, interest rate, and commodity swaps – is subject to BCRA approval.
	Sale or issue abroad by residents: Restricted.
Commercial credits	*By residents to non-residents* – Residents may make advance payments on imports to their foreign suppliers of up to 360 days. Exporters may allow their customers to pay in installments. (Subject to complex procedures).
Financial credits	*By residents to non-residents* – Residents may extend credits to non-residents within the limit for the accumulation of external assets.

Feature	**Extant Capital Restrictions**
	To residents from non-residents: Restricted
Guarantees, sureties, and financial backup facilities	*By residents to non-residents* – Non-financial private sector residents may provide financial backing within the current limits on accumulation of foreign assets.
Controls on direct investment	*Outward direct investment* – Residents may access the MULC for direct investments within the limits for accumulation of external assets.
Inward direct investment	Restricted.
Controls on liquidation of direct investment	Non-residents may access the MULC to purchase foreign exchange to transfer to their foreign bank accounts the proceeds collected in the country from sales of direct investments in the non-financial private sector and the final sale of direct investments in the country in the non-financial private sector (subject to limits).
Controls on real estate transactions	The rules governing direct investments apply.
	Purchase abroad by residents : Restricted
	Purchase locally by non-residents: Purchases of real estate in border areas by foreign investors require prior approval.
	Sale locally by non-residents: Restricted.
Controls on personal capital transactions	The rules governing legal entities apply.

Feature	**Extant Capital Restrictions**
Loans	*By residents to non-residents*: Restricted.
	To residents from non-residents: Restricted.
Provisions specific to commercial banks and other credit institutions	*Lending to non-residents (financial or commercial credits)* – Credits granted by financial intermediaries must be used in the country and must finance investment, production, commercialisation, or consumption of goods and services for internal consumption or export.
	Purchase of locally issued securities denominated in foreign exchange – There are limits on the maximum amount of securities a bank may hold from a particular issuer.
	Differential treatment of deposit accounts in foreign exchange – Reserve requirements Minimum cash requirements apply separately to each currency in which liabilities are denominated.
Investment regulations	*Abroad by banks* – Transactions are prohibited by policies on general lending.
	Open foreign exchange position limits – Complex restrictions apply.
	The limit on banks' U.S. dollar exposure is 10% of a bank's net worth.
	The absolute value of the overall net position in foreign exchange – as a monthly average of daily balances converted to pesos at the reference exchange rate – may not exceed 30% of the net liabilities of the preceding month.
	When the net foreign exchange position is positive, the amount may not exceed that proportion of liquid own resources.

Feature	Extant Capital Restrictions
Provisions specific to institutional investors	*Limits (max.) on securities issued by non-residents* – Mutual funds may invest 25% in publicly offered securities issued by non-residents; pension funds may invest up to 10%.
	Limits (max.) on investment portfolio held abroad – There is a 25% limit on investment for mutual fund portfolios, but this limit does not apply to MERCOSUR countries and Chile. For diversification, no more than 10% of pension funds may be invested in securities issued by a foreign sovereign, or in securities of foreign corporations issued abroad.
	Limits (min.) on investment portfolio held locally – When a mutual fund consists of negotiable securities, a minimum of 75% of the investment must be made in assets issued and traded in Argentina, including those issued by MERCOSUR countries and Chile.
Currency-matching regulations on assets/ liabilities composition	Apply.
Japan	
Controls on capital transactions	Apply.
Controls on direct investment	Outward direct investment: Outward direct investments by residents in a limited number of industries, such as the manufacture of arms, require prior notice. Inward direct investment : Inward direct investments by foreign investors in a limited number of industries, such as the manufacture of arms, require prior notice.

Feature	Extant Capital Restrictions
Provisions specific to institutional investors	*Limits (max.) on investment portfolio held abroad* –The limits are (1) 30% of total assets for insurance companies purchasing foreign currency– denominated assets; and (2) 20% of the reserve funds issued by non-residents for bond holdings by the Post Office Insurance Fund.
Other controls imposed by securities laws	Apply.
France	
Controls on capital transactions	Apply.
Controls on direct investment	Direct investments by companies not listed publicly are defined as those in which foreign investors together hold more than one-third of the capital. However, there are no controls on investments in a company whose capital is more than 50% foreign owned. In the case of firms whose shares are listed on the stock exchange, the threshold is also 50% of capital; this applies to each individual foreign participation but not to total foreign participation. To determine whether a company is under foreign control, the Ministry of Economy and Finance (MINEFI) may take into account any special relationships resulting from stock options, loans, patents, licenses, or commercial contracts. Inward direct investment: An authorisation is required for investments in areas pertaining to public order, public health, and defence.
Controls on liquidation of direct investment	The liquidation proceeds of foreign direct investment in France may be freely transferred abroad; the liquidation must be reported to the MINEFI within 20 days of its occurrence.

Feature	Extant Capital Restrictions
	The liquidation of direct investments abroad is free from any prior application, provided that the corresponding funds have been reported to the Bank of France.
Provisions specific to institutional investors	Currency-matching regulations on assets/liabilities composition: Insurance companies in the EU are required to cover their technical reserves with assets expressed in the same currency.
Italy	
Controls on capital and money market instruments	Apply.
On collective investment securities	*Sale or issue locally by non-residents* – The offering of securities issued by mutual funds that are not covered by EU directives is subject to authorisation.
Provisions specific to institutional investors	*Limits (max.) on securities issued by non-residents* – Portfolio investments abroad by life insurance and pension funds are subject to prudential regulations. Currency-matching regulations on assets/liabilities composition: Apply.
Other controls imposed by securities laws	The public offering in Italy of financial products is to be reported to the supervisory authority, and the corresponding prospectuses should be attached.
Australia	
Controls on capital transactions	The purchase of shares and other securities of a participatory nature, which may be affected by laws and policies on inward direct investment, may require notification to the Australian authorities. Detailed guidelines apply.

Feature	Extant Capital Restrictions
Controls on capital and money market instruments. On capital market securities, shares or other securities of a participating nature.	*Purchase locally by non-residents*: Restricted.
	Sale or issue abroad by residents: Restricted.
Bonds or other debt securities	*Sale or issue locally by non-residents*: Restricted.
On money market instruments	The regulations governing bonds or other debt securities apply.
Controls on derivatives and other instruments	An AFSL is required to purchase or sell foreign currency, except when one of the following conditions is met: (1) the transaction is settled immediately; (2) the person is not a dealer in foreign currency; (3) the person is dealing on his or her own account; or (4) it is a foreign company that is a counterparty to derivatives of foreign exchange contracts, where it is dealing or making a market in foreign exchange contracts.
	Sale or issue locally by non-residents : Restricted.
Controls on credit operations Commercial credits	*By residents to non-residents* : Restricted.

Feature	**Extant Capital Restrictions**
Controls on direct investment	*Inward direct investment*: Prior authorisation is required for (1) acquisitions by foreign investors of a substantial interest in an Australian business, (2) all investments subject to special restrictions (i.e., in the banking, civil aviation, airports, shipping, media, telecommunications, and real estate sectors), (3) direct investments by foreign governments or their agencies, irrespective of size; and (4) proposals to establish new business when the total amount of the investment is $A 10 million or more.
Controls on real estate transactions	*Purchase locally by non-residents* – All acquisitions of residential real estate, including vacant land, must be documented, unless exempt by regulation. Acquisitions of non-residential commercial real estate for development are normally approved, as are acquisitions of developed non-residential commercial real estate. Foreign acquisitions of established residential real estate are normally approved only in cases involving temporary residents who acquire the property as their principal place of residence for a period in excess of 12 months subject to resale of the property upon departure.
Controls on personal capital transactions – Gifts, endowments, inheritances, and legacies	*By residents to non-residents* – Transfers may be subject to approval of the authorities in cases where the gift involves a foreign person obtaining an interest in Australian urban land.
Provisions specific to commercial banks and other credit institutions Investment regulations	Authorised deposit–taking institutions are subject to prudential requirements, e.g., liquidity management and credit concentration. *In banks by non-residents* – Prior approval from the Treasurer is required for any person or group – domestic or foreign – to acquire a 15% or larger share in a financial sector company.

Feature	Extant Capital Restrictions
Provisions specific to institutional investors	*Limits (max.) on securities issued by non-residents* – Foreign-owned life insurance companies may operate only in the form of locally incorporated subsidiaries.
Other controls imposed by securities laws	The rules of the Australian Stock Exchange require that, to be a participating organisation of the exchange, a majority of the directors must be Australian residents.
Korea	
Controls on capital transactions	Controls on capital transactions are based on a negative list system. Proceeds from capital transactions in excess of $100,000 or its equivalent must be repatriated to Korea within six months of accrual. These funds, however, may be held abroad and used for overseas transactions in accordance with the regulations on foreign exchange transactions. Non-residents may borrow stocks from residents through brokerage houses up to the value of W 5 billion without approval from or reporting to the authorities.
Controls on capital and money market instruments	*Sale or issue locally by non-residents:* Foreign institutions are eligible to list their shares on the Korean Stock Exchange in the form of depository receipts.
On capital market securities Shares or other securities of a participating nature	Foreign Institutions are eligible to list their shares on the Korean Stock Exchange in the form of Depository Receipts.
Bonds or other debt securities	*Sale or issue locally by non-residents* – Foreign institutions may issue won-denominated bonds in the domestic capital market. However, the issuer must submit a prior report to the MOFE and the Financial Supervisory Council (FSC).

Feature	Extant Capital Restrictions
	Sale or issue abroad by residents – The sale or issuance of foreign currency–denominated bonds abroad by residents must be reported to a designated foreign exchange bank. The sale or issuance of won–denominated bonds abroad by residents must be reported to the MOFE.
On money market instruments	*Sale or issue locally by non-residents* – Only the issuance of won-denominated securities with a maturity of less than one year requires MOFE approval.
	Purchase abroad by residents – Purchases of short-term securities abroad denominated in won require BOK approval.
	Sale or issue abroad by residents – There are no controls for foreign exchange banks to issue money market instruments denominated in foreign currency in foreign money markets.
	Residents may issue money market instruments denominated in won in the foreign money markets with the approval of the MOFE.
On collective investment securities	*Sale or issue locally by non-residents* – Foreign institutions may issue collective investment securities in the domestic market, provided that they establish themselves in Korea and submit a prior report to the FSC. *Sale or issue abroad by residents* – According to the Foreign Exchange Transaction Regulation, residents may issue collective investment securities denominated in foreign currency in foreign markets. However, the issuer must submit a prior report to the designated exchange bank. Residents may issue collective investment securities denominated in domestic currency in foreign markets with the approval of the MOFE.

Feature	Extant Capital Restrictions
Controls on derivatives and other instruments	There are no controls on the trading of over the counter–related derivatives if the transactions are made through domestic foreign exchange banks. However, transactions in credit derivatives with domestic foreign exchange banks and those directly related to specific capital transactions require BOK notification. Security companies may carry out freely transactions in derivatives.
	Purchase locally by non-residents: Restricted.
	Sale or issue locally by non-residents – There are controls on all derivative transactions by non-residents involving the use of wonde nominated financing.
	Purchase abroad by residents: Restricted.
	Sale or issue abroad by residents: Restricted.
Controls on credit operations Commercial credits	*By residents to non-residents* – Commercial credits in domestic currency of more than W 1 billion, a lender requires BOK approval. In addition, commercial credits in foreign currency of more than $10 million or its equivalent by companies require BOK approval.
	To residents from non-residents – Only commercial credits with maturities of one year or less, granted to enterprises with unsound financial structures, require MOFE approval.
Financial credits	*By residents to non-residents* – Credits and loans denominated in domestic currency of more than W 1 billion, a borrower require BOK approval. In addition, commercial credits in foreign currency of more than $10 million or its equivalent by companies require BOK approval.

Feature	**Extant Capital Restrictions**
	To residents from non-residents – Only financial credits with a maturity of one year or less, granted. Guarantees, sureties, and financial backup facilities *By residents to non-residents*-Residents, other than banks, must notify or obtain approval from the BOK.
Controls on direct investment	*Outward direct investment* – Under current regulations, notification to and approval by a foreign exchange bank is required.
	Inward direct investment – All foreign direct investments, except those in industries on the negative list, are subject to a notification requirement. A notification is deemed accepted by a foreign exchange bank unless it advises to the contrary. Equity participation is possible by increasing the amount invested in newly established or existing enterprises. Direct investment by means of mergers and acquisitions is also allowed.
Controls on real estate transactions	*Purchase abroad by residents* – The acquisition of real estate for business activities and for the establishment of hospitals, schools, and religious institutions requires notification to and approval by the BOK. However, neither approval nor notification is required for the acquisition of overseas real estate by foreign exchange banks or residents if given as gifts or received through inheritance from non-residents.
	Purchase locally by non-residents – Notification to the BOK is required for the acquisition of real estate. *Sale locally by non-residents* – No controls apply if the real estate was acquired in compliance with foreign exchange regulations.

Feature	Extant Capital Restrictions
Controls on personal capital transactions	
Loans	*By residents to non-residents* – BOK approval is required for all lending by residents to non-residents. *To residents from non-residents* – Notification to the BOK is required for all lending to residents by non-residents.
Provisions specific to commercial banks and other credit institutions.	There are prudential regulations on the assets/liabilities compositions of foreign exchange banks.
Differential treatment of deposit accounts held by non-residents	*Reserve requirements* – The reserve requirements on foreign currency deposit accounts are 1%–5% for resident accounts and 1% for non-resident accounts.
	Investment regulations *In banks by non-residents* – Non-residents may acquire up to 10% of stocks without restrictions; acquisition exceeding 10% requires approval of the FSC.
	Open foreign exchange position limits – The overall net open position (short-hand position) of foreign exchange banks measured by the sum of the net short positions or the sum of the net long positions, whichever is greater, is limited to 20% of the total equity capital at the end of the previous month.
	On resident assets and liabilities: Restriction apply.

Feature	**Extant Capital Restrictions**
	On non-resident assets and liabilities – Effective January 15, 2004, the overbought or long positions of nondeliverable forwards between domestic and foreign financial institutions could not exceed 110% of the positions as of January 14, 2004.
Other controls imposed by securities laws	Controls imposed by the Securities Laws established by the FSC are as follows: (1) *domestic securities* – investments by non-resident foreign nationals are regulated by the Regulations on Securities Business, which also regulate investment ceilings, investment procedures, and the management of foreign investors; (2) *overseas securities investments* by residents are regulated by the Regulations on Securities Business, which also regulate securities' eligibility for investment and transaction procedures; and (3) *issuance of overseas securities* by residents is regulated by the Regulations on Securities Issuance and Disclosure, which also regulate the eligibility of issuers, the use of funds raised by issuance, and the obligations of issuers on reporting.
Singapore	
Controls on capital and money market instruments On capital market securities Shares or other securities of a Participating nature	*Sale or issue locally by non-residents* – Non-residents may issue equity shares. Whenever the Singapore dollar proceeds of an initial public offering by non-resident financial institutions are to be used offshore, these proceeds are no longer required to be converted into foreign currency Before their remittance abroad.

Feature	**Extant Capital Restrictions**
Bonds or other debt securities	*Sale or issue locally by non-residents* – Non-residents may issue bonds. Effective May 28, 2004, whenever the Singapore dollar proceeds are to be used offshore by non-resident financial institutions, these proceeds are no longer required to be swapped or converted into foreign currency before their remittance abroad. All rated and unrated foreign entities are allowed to issue Singapore dollar bonds. In the case of unrated foreign entities, the investor base is restricted to sophisticated investors only.
Controls on credit operations	
Financial credits	*By residents to non-residents* : Restricted.
Controls on real estate transactions	*Purchase locally by non-residents*: Foreign investment in residential and other properties, including vacant land, landed residential property, and residential property in a building of less than six floors, requires government approval. Foreigners may, however, freely purchase residential units in buildings of six or more floors and in approved condominium developments, excluding public housing. Development of land for residential purposes that has been zoned or approved for industrial or commercial use also requires government approval.
Provisions specific to commercial banks and other credit institutions	*Lending to non-residents (financial or commercial credits):* Financial institutions in Singapore may not extend Singapore dollar credit facilities exceeding S$5 million to any non-resident financial entity for speculative activities in the foreign exchange market.
Differential treatment of deposit accounts in foreign exchange	*Reserve requirements* – Foreign currency deposits of ACU member banks accepted by domestic banks are not subject to reserve requirements.

Feature	Extant Capital Restrictions
	Liquid asset requirements – Foreign currency deposits of ACU member banks accepted by domestic banks are not subject to liquid asset requirements.
Open foreign exchange position limits	No limits are set by the MAS, but it reviews the internal control systems of banks to ensure that adequate limits and controls are established for treasury activities.
Provisions specific to institutional investors	Effective August 23, 2004, risk requirements under Insurance (Valuation and Capital) Regulations 2004, which is based on the Risk Based Capital Framework, apply. The total risk requirement includes a foreign currency mismatch risk requirement of 8% on the foreign currency risk exposure. The risk requirement applies only when foreign assets are at least 10% of the total value of insurance fund assets. Insurers are also required to hold a concentration risk requirement if the foreign currency risk exposure exceeds 50% of total assets.
	Limits (max.) on securities issued by non-residents: Apply.
	Limits (max.) on investment portfolio held abroad: Apply.
	Currency-matching regulations on assets/liabilities composition: Apply.
United Kingdom	
Controls on direct investment	*Inward direct investment* – The Secretary of State for Trade and Industry may prohibit a proposed transfer of control of an important U.K. manufacturing undertaking to a non-resident when the transfer of a substantial part is considered contrary to the interests of the United Kingdom in terms of public policy, public security, or public health. If it is considered that the national

Feature	Extant Capital Restrictions
	interest cannot appropriately be protected in any other way, property in such a proposal or completed transfer may be compulsorily acquired against compensation. Both prohibition and vesting orders are subject to parliamentary approval. These powers have not been used to date.
Provisions specific to commercial banks and other credit institutions –	*Open foreign exchange position limits:* Net spot liabilities in foreign currencies (i.e., the net amount of foreign currency resources funding sterling assets) form part of a bank's eligible liabilities that are subject to a 0.15% non–interest bearing deposit requirement with the Bank of England. Effective June 1, 2004, the level of the required deposit is based on the average of reported eligible liabilities over a six-month period in excess of the equivalent of £500 million (previously, £400 million). This rule applies to building societies as well as to banks.

References and Select Bibliography on Capital Account Convertibility

Altig, David and Ed Nosal (2005), 'Dollarisation – What's in it (or not) for the issuing Country?', *Current Developments in Monetary and Financial Law,* Volume 3, International Monetary Fund (IMF), Washington D.C.

Ariyoshi, Akira, K. Habermeier, B. Laurens, I. Otker-Robe, J. I. Canales-Kriljenko and A. Kirilenko (2000), 'Capital Controls: Country Experiences with their Use and Liberalisation', *IMF Occasional Paper No. 190,* IMF, Washington D.C.

Arvai, Zsofia (2005), 'Capital Account Liberalisation, Capital Flow Patterns, and Policy Responses in the EU's New Member States', *IMF Working Paper No.213,* IMF, Washington D.C.

Bakker, Age and Bryan Chapple (2002), 'Advanced Country Experiences with Capital Account Liberalisation', *IMF Occasional Paper No. 214,* IMF, Washington D.C.

Bank Negara Malaysia (1998), *Annual Report,* Kuala Lumpur: Bank Negara Malaysia.

Bhagwati, Jagdish (1998), 'The Capital Myth – The Difference between Trade in Widgets and Dollars', *Foreign Affairs,* May/June.

Bhalla, Surjit S. (1998), 'Domestic Follies, Investment Crises: East Asian Lessons for India', Asian Security Breakfast Series at SAIS, Washington, D.C.

Bibbee, A. (2001), 'Turkey's Crisis', *OECD Observer,* May.

BIS (2003), 'China's Capital Account Liberalization: International Perspectives', *BIS papers No.15.*

Celasun, Oya (1998), 'The 1994 Currency Crisis in Turkey', *Development Research Group,* World Bank, Washington, D. C., April.

Coe, David T. and Kim Se-Jik (eds.) (2002), *Korean Crisis and Recovery*, IMF and Korea Institute for International Economic Policy, Seoul.

Das, Kaushik (2006), 'Issues and Insights – Capital account amnesia', *Business Standard,* May 31.

Daseking, Christina, Atish Ghosh, Timothy Lane, and Alun Thomas (2004), 'Lessons from the Crisis in Argentina', *Occasional Paper 236,* IMF, Washington D.C.

Deutsche Bank Research (2005), 'Global Risk Analysis: China-India Chartbook', October 10.

Draghi, Mario and Robert Pozen (2003), 'US-EU Regulatory Convergence: Capital Markets Issues', *Discussion Paper No. 444,* Harvard Law School, Cambridge.

Duttagupta, Rupa, Gilda Fernandez and Cem Karacadag (2004), 'From Fixed to Float: Operational Aspects of Moving Toward Exchange Rate Flexibility', *IMF Working Paper No.126,* IMF, Washington D.C.

Eichengreen, Barry, Michael Mussa and others (1998), 'Capital Account Liberalisation - Theoretical and Practical Aspects', *IMF Occasional Paper No.172*, IMF, Washington D.C.

Epstein, Gerald, Ilene Grabel and Jomo, K.S. (2004), 'Capital Management Techniques in Developing Countries: An Assessment of Experiences from the 1990s and Lessons for the Future', *G-24 Discussion Paper Series No. 27,* United Nations.

European Community (2002), *Consolidated Version of the Treaty Establishing the European Community*, Official Journal C 325, December 24.

Farrell, Diana and Susan Lund (2006), 'Reforming India's Financial System', *The Online Journal of McKinsey & Co.*

Fischer, Stanley, Richard N. Cooper *et al* (1998), 'Should the IMF Pursue Capital-Account Convertibility?', *Essays in International Finance No. 207,* International Finance Section, Department of Economics, Princeton University, New Jersey.

Folkerts-Landau, David, and Takatoshi Ito (1995), *International Capital Markets: Developments, Prospects, and Policy Issues*, IMF, Washington, D.C.

Fraga, Arminio (2000), 'Monetary Policy During the Transition to a Floating Exchange Rate: Brazil's Recent Experience', *Finance & Development,* March.

Ghosh, Atish and Timothy Lane (2002), 'IMF-Supported Programs in Capital Account Crises', *IMF Occasional Paper 210,* IMF, Washington D.C.

Gopinath, Shyamala (2006), 'Approach to Basel II', Address at the IBA briefing session on "Emerging Paradigms in Risk Management", Bangalore, May 12.

Goswami, S. (2006), 'CAC needs policy underpinning', *Business Line,* May 27.

Government of India (2005), *Report of the Expert Group on Encouraging FII Flows and Checking the Vulnerability of Capital Markets to Speculative Flows* (Chairman: Shri Ashok K. Lahiri), Ministry of Finance, November.

Government of India (2006), *Report of the High Level Expert Committee on Corporate Bonds and Securitization,* (Chairman: Dr. R. H. Patil).

Gupta, Desh and Milind Satheya (2004), "Financial Developments in India: Should India introduce capital account convertibility?" University of Canberra, April.

Humber, Yurly (2006), 'Much-Maligned Ruble Finally Going Global', *The Moscow Times,* June 29.

IMF (2000), 'Capital Controls: Country Experiences with their use and Liberalization', *IMF Occasional Paper 190,* IMF, Washington, D.C.

IMF (2000), 'Exchange Rate Regimes in an Increasingly Integrated World Economy', *IMF Occasional Paper No.193,* IMF, Washington, D.C.

IMF (2005), *Annual Report on Exchange Arrangements and Exchange Restrictions,* Washington, D.C.

IMF (2006), *Public Information Notice (PIN) No.06/93,* Washington, D.C. July.

Independent Evaluation Office (IEO) of the IMF (2003), *Evaluation Report on The IMF and the Recent Capital Account Crisis – Indonesia, Korea, Brazil,* Washington, D.C.

Independent Evaluation Office (IEO) of the IMF (2005), *Report on the*

Evaluation of the IMF's Approach to Capital Account Liberalization, April 20, Washington, D.C.

Ishii, Shogo and Karl Habermeier (2002), 'Capital Account Liberalization and Financial Sector Stability', *IMF Occasional Paper 211*, IMF, Washington, D.C.

Ize, Alain and Andrew Powell (2004), 'Prudential Responses to De Facto Dollarization', *IMF Working Paper No.66*, IMF, Washington, D.C.

Johnston, R. Barry, Salim M. Darbar and Claudia Echeverria (1997), 'Sequencing Capital Account Liberalization: Lessons from the Experiences in Chile, Indonesia, Korea and Thailand', *IMF Working Paper No*.157, IMF, Washington D.C.

Joshi, Vijay (2003), 'Financial Globalisation, Exchange Rates and Capital Controls in Developing countries', Merton College, Oxford.

Kapur, Basant K. (2005), 'Capital Flows and Exchange Rate Volatility: Singapore's Experience', Department of Economics, National University of Singapore.

Kawai, Masahiro, Richard Newfarmer and Sergio L Schmukler (2003), 'Financial Crises: Nine Lessons from East Asia', *Finance Working Papers No. 482*, East Asian Bureau of Economic Research, May.

Kim, Woochan and Yangho Byeon (2001), 'Restructuring Korean Banks' Short-term Debts', Conference on *Korean Crisis and Recovery,* IMF and Korea Institute for International Economic Policy, Seoul, Korea, May 17-19.

Kohli, Renu (2005), *Liberalizing Capital Flows: India's Experiences and Policy Issues,* Oxford University Press, New Delhi.

Kose, M. Ayhan, Eswar S. Prasad and Marco E. Terrones (2003), 'Financial Integration and Macroeconomic Volatility', *IMF Working Paper No.50*, IMF, Washington, D.C.

Larrain, Felipe B. and Andres Velasco (2001), 'Exchange Rate Policy in Emerging-Market Economies: The Case for Floating', *Essays in International Economics No. 224,* International Economics Section, Department of Economics, Princeton University, New Jersey.

Lau, Lawrence J. (2001), 'Lessons from the East Asian Currency Crisis and Recovery', Stanford University, January.

Laurens, Bernard J. (2005), 'Monetary Policy Implementation at Different Stages of Market Development', *IMF Occasional Paper No.244*, IMF, Washington, D.C.

Lindgren, Carl-Johan, Tomás J.T. Baliño, Charles Enoch, Anne-Marie Gulde, Marc Quintyn, and Leslie Teo (1999), 'Financial Sector Crisis and Restructuring: Lessons from Asia', *IMF Occasional Paper No. 188,* Washington, D.C.

Lipschitz, Leslie, Timothy Lane and Alex Mourmouras (2002), 'Capital Flows to Transition Economies: Master or Servant?', *IMF Working Paper, No.11*, IMF, Washington, D.C.

Lipscomb, Laura (2005), 'An Overview of Non-Deliverable Foreign Exchange Forward Markets,' Federal Reserve Bank of New York, May 8.

Lu, Ding (2006), 'China's Banking Sector Meeting the WTO Agenda', *Discussion Paper 5,* China Policy Institute, April.

Madgavkar, Anu, Leo Puri and Joydeep Sengupta (2006), 'Revitalizing India's Banks', *The Online Journal of McKinsey & Co,* June 6.

Magud, Nicolas and Carmen M. Reinhart (2005), 'Capital Controls: An Evaluation', Paper for the NBER's International Capital Flows Conference, June 2.

Martinez, Guillermo Ortiz (1998), 'What Lessons Does the Mexican Crisis Hold for Recovery in Asia?' *Finance & Development,* March.

Mecklai, Jamal (2006), 'Who's afraid of convertibility', *Business Standard,* May 5.

Mohan, Rakesh (2006), 'Coping with Liquidity Management in India: A Practitioner's View', Address at IGIDR on March 27.

Mohan, Rakesh (2006), 'Evolution of Central Banking in India', Lecture delivered at the Seminar organised by London School of Economics and the National Institute of Bank Management at Mumbai, January 24.

Mohan, Rakesh (2006), 'Financial Sector Reforms and Monetary Policy:

The Indian Experience', Paper presented at the Conference on Economic Policy in Asia at Stanford organised by Stanford Center for International Development and Stanford Institute for Economic Policy Research, June 2.

Mohan, Rakesh (2006), 'Recent Trends in the Indian Debt Market and Current Initiatives', Lecture delivered at the Fourth India Debt Market Conference and Annual Conference of FIMMDA, January 31.

Montiel, Peter J. (2005), 'Public Debt Management and Macroeconomic Stability: An Overview', *The World Bank Research Observer, Vol. 20, No.2*.

Mosnews (2006), 'Russia to Lift All Currency Controls on July 1 to make Ruble Fully Convertible', May 31.

Noland, Marcus (2005), 'South Korea's Experience with International Capital Flows', Institute for International Economics, Washington D.C.

Ocampo, Jose Antonio (2003), 'Capital Account and Counter-cyclical Prudential Regulations in Developing Countries', *Informes y estudios Especiales Serie*, Economic Commission for the Latin America and the Caribbean, United Nations, Chile.

OECD (2003), 'Attracting Investment to China', *Policy Brief, OECD Observer.*

Patra, M.D., S. Pattanaik and S. Sahoo (1999), 'Asian Financial Crisis: Issues and Lessons', *RBI Staff Studies*, August.

PIB Press Release (2006), 'PM's Address to the Annual General Meeting of ADB', May 5.

PIB Press Release (2006), 'Finance Minister Inaugurates Advantage India Function', May 4.

PIB Press Release (2006), 'FM's Address at the Board of Governors AGM of ADB', May 5.

PIB Press Release (2006), 'FM's Speech in the Governors' Seminar on 'A Shared Responsibility: Fixing Global Payments Imbalances', May 4.

PIB Press Release (2006), 'FM's Statement at Business Session of Board of Governors of ADB', May 6.

Prasad, Eswar S. and Raghuram G. Rajan (2005), 'Controlled Capital Account Liberalisation: A Proposal', *IMF Policy Discussion Paper No.7,* IMF, Washington, D.C.

Prasad, Eswar S. and Shang-Jin Wei (2005), 'The Chinese Approach to Capital Inflows: Patterns and Possible Explanations', *IMF Working Paper No. 79*, IMF, Washington, D.C.

Prasad, Eswar S., Kenneth Rogoff, Shang-Jin Wei and M. Ayhan Kose (2003), 'Effects of Financial Globalisation on Developing Countries', *IMF Occasional Paper No. 220,* IMF, Washington, D.C.

Rajan, Raghuram G. (2006), 'Making India a Global Hub', *The Online Journal of McKinsey & Co,* June 3.

Ranade, Ajit and Gaurav Kapur (2003), 'Appreciating Rupee: Changing Paradigm?', *Economic and Political Weekly,* February 22.

Rangarajan, C. and A. Prasad (1999), 'Capital Account Liberalisation and Controls – Lessons from the East Asian Crisis', *ICRA Bulletin – Money and Finance*, April-June.

Rao, S. L. (2006), 'Debating a Bad Idea – There is No Merit in Full Rupee Convertibility at Any Time' *The Telegraph,* May 8.

Raychaudhuri, Bijoy (2003), 'Financial Liberalisation and the Economic Crisis in Asia', *Asia-Pacific Development Journal,* June.

Reddy, Y.V. (2004), 'Capital Account Liberalisation and Capital Controls', Address at the Central Bank Governors Symposium convened by the Bank of England in London on June 25.

Reddy, Y.V. (2006), 'Challenges and Implications of Basel II for Asia', Address at the Asian Development Bank's 39th Annual Meeting of the Board of Governors at Hyderabad on May 3.

Reddy, Y.V. (2006), 'Reflections on India's Economic Development', Address at the Council on Foreign Relations, New York, May 12.

Reddy, Y.V. (2006), 'Reforming India's Financial Sector: Changing Dimensions and Emerging Issues', Address at the International Centre for Monetary and Banking Studies, Geneva.

Reserve Bank of India (2000), *'Report of The Advisory Group on*

Transparency in Monetary and Financial Policies', (Chairman: Shri M. Narasimham) Standing Committee on International Financial Standards and Codes, Mumbai.

Reserve Bank of India (2003), *Report of the Working Group on Instruments of Sterilisation,* Mumbai.

Reserve Bank of India (2005), 'Revision of NEER and REER Indices', *RBI Bulletin,* December.

Reserve Bank of India, *Report on Currency and Finance*, 2001-02, 2002-03, 2003-04.

Roach, Stephen (2006), 'Global Imbalances Matter More than Ever', *morganstanley.com,* May 5.

Rodrik, Dani (1998), 'Who needs Capital Account Convertibility?', *Essay in International Finance*, Princeton University, February.

Schneider, Benu (2000), 'Issues in Capital Account Convertibility in Developing Countries', Prepared for Overseas Development Institute (ODI) Conference on 'Capital Account Liberalisation: The Developing Country Perspective' ODI, London, June.

Schneider, Benu (2005), 'Do Global Standards and Codes Prevent Financial Crises? Some Proposals on Modifying the Standards-Based Approach', *Discussion Paper No.177,* United Nations Conference on Trade and Development, United Nations, April.

Sen, Pronab, Ashima Goyal and Srinivasan Varadarajan (2006): 'Full Rupee Convertibility: Good, bad or ugly?', *The Economic Times*, March 28.

Sen, Sunanda (2006), 'Drive with Caution' *The Telegraph*, May 9, 2006.

Subbulakshmi, V. (2004), *Capital Account Convertibility: An Introduction*, ICFAI University Press, Hyderabad.

Subbulakshmi, V. (2004), *Capital Account Liberalisation – Asian Experience*, ICFAI University Press, Hyderabad.

Subbulakshmi, V. (2004), *Capital Account Liberalisation – Latin American Experience*, ICFAI University Press, Hyderabad.

Sundararajan, V. Akira Ariyoshi and Inci Otker-Robe (2000), 'International Capital Mobility and Domestic Financial System Stability: A Survey of Issues', Seminar on Financial Risks, System Stability, and Economic Globalization, June 5–8, IMF, Washington, D.C.

Tee, Ong Chong (2001), 'Singapore's Policy of Non-internationalisation of the Singapore Dollar and the Asian Dollar Market', *BIS Paper No.15.*

US Treasury (2006), *Report on International Economic and Exchange Rate Policies,* May.

Venkatesh, M. R. (2006), 'Full Convertibility Demands a Re-think of Policy Calculus', *Business Line,* May 19.

Westin, Peter (2006), 'Capital Account Convertibility in Sight', Prime-Tass News Agency, May 27.

Williamson, John (2000), 'Issues Regarding the Composition of Capital Flows', Prepared for ODI Conference on 'Capital Account Liberalisation: The Developing Country Perspective' in London, June.

Williamson, John and Molly Mahar (1998), 'A Survey of Financial Liberalisation', *Essays in International Finance No. 211*, International Finance Section, Department of Economics, Princeton University, New Jersey.

Williamson, John, Amitava Krishna Dutt and others (2006), 'Capital Account Convertibility - A Debate', *Economic and Political Weekly,* May 13.

Yesuthasen, P. (2006), 'Road to Freedom: Capital Account Convertibility', *Economic Times*, May 10.