THE WALL STREET JOURNAL.
WSJ.com

ASIA NEWS | July 18, 2013, 12:10 p.m. ET

G-20 Readies Financial Safety Nets

By NATASHA BRERETON-FUKUI

MOSCOW—The Group of 20 industrialized and developing countries is focusing this week on safety nets as the prospect of a rollback of monetary stimulus in the U.S. raises concerns of a stampede of funds out of emerging markets.

But progress could be stymied by lingering resentment in some G-20 countries toward the International Monetary Fund.

Finance ministers and central bankers from the G-20 meeting in Moscow on Friday and Saturday were due to consider ways to improve cooperation between the IMF and regional safety nets—crisis-financing arrangements such as currency-swap agreements to deal with localized shocks—ahead of a leaders' summit in September.

Other topics on their agenda include tax avoidance, long-term investment financing, financial regulation and deficit reduction.

Indications that the Federal Reserve will soon start to reduce the amount of assets it buys to stimulate the U.S. economy have already sparked sharp falls in emerging market currencies, bonds and equities. That has heightened fears that the outflow could become a torrent when the Fed actually starts to retract its stimulus program, known as quantitative easing.

In an interview, South Korean Finance Minister Hyun Oh-seok said it was important that countries had policies ready to cope with market volatility. But individual action may not be enough to deal with a particularly large shock, he said, in which case regional financial safety nets could be crucial.

"As we face the possible unwinding of quantitative easing, I believe that this issue could play a very important role," Mr. Hyun said.

He plans to propose to the G-20 that a channel be set up among regional safety nets to facilitate the exchange of experience and information. Further discussion is needed on how best to increase collaboration between the IMF and regional facilities, while taking their diverse characteristics into account, he said.

The Brazilian real collapsed 4.2% against the dollar after Fed chairman Ben Bernanke last month indicated the central bank would scale back its bond purchases. The Indian rupee dropped 4.1%, although its decline was exacerbated by domestic factors. Other Asian currencies were also hit, with the Korean won falling 2.8%, the Thai baht 2.6% and the Malaysia ringgit 2.2%.

"There is no doubt that asset bubbles are present in many Southeast Asian economies and a sudden reversal of capital flows could result in serious liquidity concerns," said Jayant Menon, lead economist for trade and regional cooperation in the Asian Development Bank's office of regional economic integration.

In an April policy paper, the IMF identified ways to advance cooperation with regional financial safety nets. These included collaboration in policy monitoring and information sharing and streamlining the IMF's approach to ensure equal treatment.

"The IMF is eager to develop a framework for engaging with regional financing arrangements, to ensure that it sticks to its own lending guidelines and maintains leverage in getting countries to adopt better policies," said Eswar Prasad, a professor at Cornell University and formerly a senior IMF official.

He noted that linking regional safety nets to the IMF—as is the case for Asia's Chiang Mai Initiative Multilateralization, or CMIM—could boost their firepower and credibility.

The CMIM offers a portion of its credit without requiring the country in question to enter into a program with the fund. Some other regional facilities, such as the Arab Monetary Fund and the Latin American Reserve Fund, currently have no explicit link with the IMF.

"One downside of a formal link to the IMF is that countries may then prefer to continue self-insuring by building up foreign exchange reserves rather than subject themselves, even indirectly, to conditions imposed by the IMF," Mr. Prasad said.

That attitude has been borne of the experience of various countries in times of turmoil.

Asia's safety net was set up in response to the late-nineties financial crisis, during which South Korea and Thailand had little choice but to accept what they viewed to be overly strict IMF austerity plans in exchange for financial aid. Malaysia rejected IMF help and took its own path, including implementing strict capital controls and structural reforms.

More recently, Asian officials have been working to beef up the Chiang Mai Initiative's surveillance capabilities and increase the funding it can supply without IMF involvement.

In Europe, there has been a backlash against the IMF after it criticized the European Commission's handling of the Greek debt crisis. Klaus Regling, who heads the European Stability Mechanism—the euro zone's permanent bailout fund—told Germany's Frankfurter Allgemeine Zeitung last month he would like to see the IMF gradually phased out of European bailouts.

While such sentiments may present a hurdle to the G-20's goal of increasing the IMF's involvement in regional arrangements, rejecting the fund's support entirely isn't an option for Asia at least, said Hal Hill, professor of Southeast Asian economies at Australian National University.

"Like it or not—and many don't—the IMF is still the only game in town with a coherent analytical framework, and an operational system that is up and running," he said.

—Ewen Chew contributed to this article.

Write to Natasha Brereton-Fukui at natasha.brereton@dowjones.com