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Chapter 1 : The new wave of private capital inflows : push or pull? (English) | The World Bank

The new wave of private capital inflows: push or pull? (English) Abstract. Widespread private capital inflows to middle-income countries have surged over the past three years.

Eduardo Fernandez-Arias Abstract Widespread private capital inflows to middle-income countries have surged over the past three years. At the same time, Brady-type debt reduction operations and domestic policy reform took place, indicators of country creditworthiness improved dramatically, and international interest rates plummeted. Which factors most fully explain the wave of capital inflows? How sustainable is it? Some see this new wave of voluntary capital inflows as being mostly"pulled"by attractive domestic conditions, which open new and profitable investment opportunities in the domestic economy and improve country creditworthiness. Under this interpretation, if successful domestic policies are maintained, capital inflows will be sustained. Others see these inflows as being mostly"pushed"by conditions especially low interest rates in industrial countries. Under this interpretation, capital inflows would diminish and possibly turn to outflows if international real interest rates returned to the higher levels of the s. The author presents an analytical model of international portfolio investment in developing countries based on non-arbitrage conditions between external returns and domestic returns adjusted by country risk. The author uses the model to explain why the new wave of private capital inflows is mostly a middle-income country phenomenon. To analyze the issue of private capital inflows, he applies the model of data for a representative panel of middle-income countries. The main empirical result is that except in Argentina, the Republic of Korea, and notably, Mexico , the surge of capital inflows appears to be driven more by low returns in industrial countries than by domestic factors. So recent levels of capital inflows would be unsustainable if global interest rates returned soon to higher levels and cautious policies should be followed. Two other important conclusions are obtained. First, depressed returns in industrial countries caused the improved creditworthiness in indebted countries through their effects on discount rates. Country creditworthiness was an important transmission mechanism for external shocks and is the key to reconciling the push and pull interpretations of market data. Second, a soft landing appears feasible. Stock adjustment does not appear to be a significant component of the adjustment mechanism manifested in the surge of capital inflows. In other words, the evidence so far suggests that gradual increase in international interest rates would result in less capital inflow, or moderate capital outflows in some countries, rather than massive capital outflows that quickly bring down the stock of foreign liabilities. By and large, if there are capital outflows, they are unlikely to match past inflows unless the reversal in external conditions coincides with a worsening of domestic conditions.

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Chapter 2 : Prepared for the Seminar The New Wave of Capital Inflows: - CORE

Some see this new wave of voluntary capital inflows and rapidly improving creditworthiness as evidence that debt strategies have worked and domestic policies are on the right track. In this view, domestic factors are more important than extemal factors in explaining these inflows.

Stiglitz - World Development , " The world is just emerging from the worst financial and economic crisis since the great Depression. In matters were only slightly better. Elsewhere, matters are even bleaker: Indonesia remains in depression, civil unrest affecting many of its far-flung islands. While exchange rates have stabilized in East Asia, other financial variables, like stock prices, have not fared so well, and unemployment remains far higher than before the crisis, and real wages far lower. Elsewhere, large parts of the world remain in a precarious economic positionâ€"with deep recession or depression facing several countries in Latin America, and output in many of the economies in transition still markedly below what it was a decade ago. Sovereign borrowing by developing countries: What determines market access? Working Papers describe research in progress by the author s and are published to eli Working Papers describe research in progress by the author s and are published to elicit comments and to further debate. What determines the ability of governments from developing countries to access international credit markets? We examine this question using detailed data on sovereign bond issuances and public syndicated bank loans since We are unable to detect strong punishment of defaulting countries by credit markets. This paper analysis the unparalleled increase in foreign direct investment to emerging market economies of the last 25 years in connection to the recent process of integration of these economies into world capital markets. Our findings are broadly consistent with the hypothesis of market integrat Our findings are broadly consistent with the hypothesis of market integration. First, global factors i. We investigate the wave of privatizations in emerging economies as an alternative explanation for the growth in foreign direct investment. We also discuss the policy implications of our results. Currency Crashes in Emerging Markets: Empirical Indicators by Jeffrey A. Rose - Journal of International Economics , " We use a panel of annual data for over one hundred developing countries from through to characterize currency crashes. We define a currency crash as a large change of the nominal exchange rate that is also a substantial increase in the rate of change of nominal depreciation. We examine the composition of the debt as well as its level, and a variety of other macroeconomic factors, external and foreign. Crashes tend to occur when: A low ratio of FDI to debt is consistently associated with a high likelihood of a crash. This paper -- a product of the International Finance Division, International Economics Department -- is part of a larger effort in the department to analyze policy implications of private capital flows to developing countries. Copies of the paper are available free from the World Bank, H Street Please contact Rose Vo, room , telephone , fax , Internet address hvol worldbank. An objective of the sertes is roger the findings out qu,ckly, even: The papers carry the names of the authors and should be used and cited accordingly. Working Papers describe research in progress by the author s and are published t The results suggest that China did not have much impact on FDI to other countries. In particular, low-income economies, which compete with China for low-wage investment, and countries with low levels of education or scientific development do not seem to have been especially affected. Show Context Citation Context Country dummies capture country-specific effects. Taxes on foreign investment would have beensrelevant as well, but little data are available. Rising international bank financing to developing countries has motivated a debate on the behavior of these claims. We find that banks transmit shocks from their home countries and changes in the We find that banks transmit shocks from their home countries and changes in their claims on other countries spill over to individual hosts. Finally, foreign bank lending reacts more to positive than to negative host shocks and is not significantly curtailed during crises. We would like to thank the Bank for International Settlements for providing us data and, in particular, Jesper Wormstrup at this institution for answering many questions on this dataset. The findings, interpretations, and conclusions expressed in this paper are entirely those of the authors and do not necessarily represent the views of the World Bank, its Executive Directors, or the countries they represent.

Chapter 3 : The new wave of private capital inflows : push or pull?

Will capital inflows boom again in Latin America as countries recover from the recession? And will they bust again shortly thereafter, repeating the cycle of the past? Is there something fundamentally different about the new wave of capital inflows to alter this historical pattern, a sea change in the way the region is financially.

The new wave of private capital inflows: English Abstract Widespread private capital inflows to middle-income countries have surged over the past three years. At the same time, Brady-type debt reduction operations and domestic policy reform took place, indicators of country creditworthiness improved dramatically At the same time, Brady-type debt reduction operations and domestic policy reform took place, indicators of country creditworthiness improved dramatically, and international interest rates plummeted. Which factors most fully explain the wave of capital inflows? How sustainable is it? Some see this new wave of voluntary capital inflows as being mostly "pulled" by attractive domestic conditions, which open new and profitable investment opportunities in the domestic economy and improve country creditworthiness. Under this interpretation, if successful domestic policies are maintained, capital inflows will be sustained. Others see these inflows as being mostly "pushed" by conditions especially low interest rates in industrial countries. Under this interpretation, capital inflows would diminish and possibly turn to outflows if international real interest rates returned to the higher levels of the s. The author presents an analytical model of international portfolio investment in developing countries based on non-arbitrage conditions between external returns and domestic returns adjusted by country risk. The author uses the model to explain why the new wave of private capital inflows is mostly a middle-income country phenomenon. To analyze the issue of private capital inflows, he applies the model of data for a representative panel of middle-income countries. The main empirical result is that except in Argentina, the Republic of Korea, and notably, Mexico , the surge of capital inflows appears to be driven more by low returns in industrial countries than by domestic factors. So recent levels of capital inflows would be unsustainable if global interest rates returned soon to higher levels and cautious policies should be followed. Two other important conclusions are obtained. First, depressed returns in industrial countries caused the improved creditworthiness in indebted countries through their effects on discount rates. Country creditworthiness was an important transmission mechanism for external shocks and is the key to reconciling the push and pull interpretations of market data. Second, a soft landing appears feasible. Stock adjustment does not appear to be a significant component of the adjustment mechanism manifested in the surge of capital inflows. In other words, the evidence so far suggests that gradual increase in international interest rates would result in less capital inflow, or moderate capital outflows in some countries, rather than massive capital outflows that quickly bring down the stock of foreign liabilities. By and large, if there are capital outflows, they are unlikely to match past inflows unless the reversal in external conditions coincides with a worsening of domestic conditions.

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Chapter 4 : The new wave of private capital inflows: Push or pull? - CORE

This paper studies the determinants and sustainability of the widespread private capital inflows to middle-income countries after The key question is whether these flows are mostly 'pulled.

References Capital flows between countries can yield significant benefits. They allow investors to diversify their risks and increase returns, and they allow residents of recipient countries to finance rapid rates of investment and economic growth, as well as to increase consumption. However, sudden shifts in capital flows can be devastating for recipient countries. This experience, shared to varying degrees by a number of other developing countries in the s, illustrates the importance of understanding the factors that explain capital flows to developing countries. This Economic Letter reviews some of the stylized facts of capital flows in the s and discusses factors that may account for their behavior. Capital flows to developing countries As the figure illustrates, there has been a strong upward trend in capital flows since the s, despite recent reversals. At the same time, the figure shows that capital flows are distinctly cyclical: A boom in capital flows to developing countries in the s was followed by a sharp reversal in the s. Another much larger boom and reversal occurred in the s. Finally, the figure reveals dramatic changes in the composition of capital flows. Bank lending and other flows which largely reflect bank loans dominated capital flows to developing countries in the s, while foreign direct investment and portfolio investment dominated such flows in the s. However, it is apparent from the figure that even in the s, capital flow reversals largely reflected the sudden interruptions in bank lending associated with the Mexican crisis of and the East Asian crises of Trend factors The dramatic increase in international capital flows in the s reflects the opening of two major pathways to international portfolio diversification. First, developing countries have encouraged globalization by liberalizing their domestic financial markets and opening them to foreigners. Developing countries also have expanded investment opportunities by privatizing government enterprises and encouraging the development of deeper and more liquid financial markets. Second, advances in information and communications technology have made it much easier to evaluate and monitor investments around the globe. Lack of information about the quality of investment projects has traditionally discouraged cross-border lending by creating greater incentives for borrowers with very risky projects to apply for financing a phenomenon known as adverse selection. This problem is particularly severe in developing countries, where reporting and accounting practices are generally less transparent. Lending also may be limited because borrowers can shift part of the risk of their projects to lenders, creating an incentive for borrowers to engage in riskier activities once they have received credit this is known as moral hazard. In addition to attenuating these effects, technological advances also have contributed to the development of financial instruments that more effectively manage risk, and also make it easier to circumvent remaining barriers to foreign investment. Such advances also may have reduced the comparative advantage of banks in obtaining information about the quality of borrowers, contributing to the observed decline in the importance of bank lending in international capital flows. Even with the sharp increases in capital flows in the s, international portfolio diversification is far from complete. Standard models of capital asset pricing imply that investors seeking to diversify their portfolios should hold equities in different markets roughly in proportion to the share of these markets in total market capitalization. The home bias in bond markets is even greater: Similar home bias in investment occurs in other countries. However, apart from impediments to market access and difficulties in assessing and monitoring investments cited earlier, exchange rate uncertainty is likely to have played an important role. This is suggested by the wave of cross-border mergers and acquisitions observed in Europe since the introduction of its common currency, the euro, which eliminated currency risk in that region. For example, better macroeconomic policies encouraged capital flows into developing countries in the s, contributing to economic booms. However, the perception that governments in recipient countries would prop up the financial sector in case of adverse outcomes encouraged excessive risk-taking as reflected in declining foreign reserve cover for the short-term liabilities of the financial system and in lending to highly volatile and ultimately unproductive sectors. The resulting financial fragility made these economies vulnerable to sudden changes in investor sentiment and capital flow reversals. The relative importance of external or domestic factors in driving capital flows has important implications for policy. If capital flows are driven largely by domestic factors, developing countries can attract a steady and predictable flow of foreign capital and minimize cycles by adopting sound macroeconomic and financial policies. However, if capital flows are driven largely by external factors, developing countries are vulnerable to unexpected external shocks even if they maintain prudent policies, and they must take measures to insulate themselves. Research suggests that both external and domestic factors contribute to capital flows, but their relative importance appears to vary over time. Calvo, Leiderman, and Reinhart found that declines in U. However, domestic factors apparently became more important determinants of capital flows in World Bank , as rising U. Indeed, the negative correlation between capital flows and U. Taking a longer perspective, Milesi-Ferretti and Razin studied sudden reversals in capital inflows in 86 countries from and found that both external and domestic factors, particularly those affecting the sustainability of external borrowing, play a role in explaining sudden reversals of capital inflows as measured by an increase in the current account of a recipient country. External factors that increase the likelihood of capital flow reversals include worsening terms of trade the ratio of export to import prices , high U. Among the domestic factors likely to be associated with a reversal in capital inflows are larger current account deficits or foreign borrowing, a smaller ratio of exports plus imports to GDP, lower foreign reserves, and a smaller proportion of concessional debt. Additional perspectives on the causes of sudden capital inflow reversals are provided by the literature on currency crises. Moreno and Trehan found that global and regional shocks explain a large proportion of the global incidence of sharp depreciation episodes over the period However, a study by Berg and Pattillo suggests that domestic factors may have played a larger role in the most recent East Asian currency crises that began in Conclusions International capital flows appear to be driven in part by growing international portfolio diversification, which is still at an early stage. Capital flows also are influenced by global and domestic factors whose relative importance tends to vary over time. While capital flows provide significant benefits to investors and recipients, their sensitivity to economic conditions makes recipient countries vulnerable to sudden reversals. Developing countries thus face the challenge of designing economic policies that secure the most benefits from capital inflows while reducing their vulnerability to sudden reversals. Countries have sought to reduce vulnerability in several ways. Some have adopted more flexible exchange rates, which tend to dampen boom and bust cycles by regulating the volume of capital flows. Others have strengthened their domestic financial systems to improve the intermediation of sudden capital inflows or to cope with sudden capital outflows. In a number of cases, countries have restricted capital inflows or outflows. Moreno, Ramon, and Bharat Trehan. Private Capital Flows to Developing Countries. The Road to Financial Integration. This publication is edited by Sam Zuckerman and Anita Todd. Permission to reprint must be obtained in writing.

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Chapter 5 : Formats and Editions of The new wave of private capital inflows : push or pull? [www.nxgvision

"Prepared for the Seminar "The New Wave of Capital Inflows: Sea Change or Just Another Tide" Annual Meetings of the Board of Governors, Inter- American Development Bank and Inter.

The new wave of private capital inflows: At the same time, Brady-type debt reduction operations and domestic policy reform took place, indicators of country creditworthiness improved dramatically At the same time, Brady-type debt reduction operations and domestic policy reform took place, indicators of country creditworthiness improved dramatically, and international interest rates plummeted. Which factors most fully explain the wave of capital inflows? How sustainable is it? Some see this new wave of voluntary capital inflows as being mostly "pulled" by attractive domestic conditions, which open new and profitable investment opportunities in the domestic economy and improve country creditworthiness. Under this interpretation, if successful domestic policies are maintained, capital inflows will be sustained. Others see these inflows as being mostly "pushed" by conditions especially low interest rates in industrial countries. Under this interpretation, capital inflows would diminish and possibly turn to outflows if international real interest rates returned to the higher levels of the s. The author presents an analytical model of international portfolio investment in developing countries based on non-arbitrage conditions between external returns and domestic returns adjusted by country risk. The author uses the model to explain why the new wave of private capital inflows is mostly a middle-income country phenomenon. To analyze the issue of private capital inflows, he applies the model of data for a representative panel of middle-income countries. The main empirical result is that except in Argentina, the Republic of Korea, and notably, Mexico , the surge of capital inflows appears to be driven more by low returns in industrial countries than by domestic factors. So recent levels of capital inflows would be unsustainable if global interest rates returned soon to higher levels and cautious policies should be followed. Two other important conclusions are obtained. First, depressed returns in industrial countries caused the improved creditworthiness in indebted countries through their effects on discount rates. Country creditworthiness was an important transmission mechanism for external shocks and is the key to reconciling the push and pull interpretations of market data. Second, a soft landing appears feasible. Stock adjustment does not appear to be a significant component of the adjustment mechanism manifested in the surge of capital inflows. In other words, the evidence so far suggests that gradual increase in international interest rates would result in less capital inflow, or moderate capital outflows in some countries, rather than massive capital outflows that quickly bring down the stock of foreign liabilities. By and large, if there are capital outflows, they are unlikely to match past inflows unless the reversal in external conditions coincides with a worsening of domestic conditions.

Chapter 6 : The New Wave of Capital Inflows: Sea Change or Tide? - CORE

Abstract. This paper was prepared for the Seminar The New Wave of Capital Inflows: Sea Change or Tide? Annual Meetings of the Board of Governors, Inter-American Development Bank and Inter-American Investment CorporationWill capital inflows boom again in Latin America as countries recover from the recession?

Chapter 7 : The new wave of private capital inflows : push or pull? (InglÃªs) | Banco Mundial

The author uses the model to explain why the new wave of private capital inflows is mostly a middle-income country phenomenon. To analyze the issue of private capital inflows, he applies the model of data for a representative panel of middle-income countries.

Chapter 8 : The New Wave of Capital Inflows: Sea Change or Tide?

Will capital inflows boom again in Latin America as countries recover from the recession? And will they bust again *shortly thereafter, repeating the cycle of the past? Is there something fundamentally different about the new wave of capital inflows to alter this historical pattern, a sea.*

Chapter 9 : CiteSeerX â€" Citation Query The New Wave of Private Capital Inflows: Push or Pull

lend stability to the new wave of capital inflows. This paper addresses issues concerning the future of capital inflows to Latin America by examining the factors that may lead to a structural change with the past.