International Capital Flows: General Discussion

In the general discussion, **Robert Chandross** noted that in the debate on the merits of capital controls, it is often overlooked that, in several of the crisis-hit economies, outflows of resident funds were a dominant force in the crisis. Moreover, he suggested that Chile might not be representative of emerging economies since its high credit rating makes international investors willing to maintain long-term positions in the country even when controls on short-term flows are present. Instead, in the typical emerging country with a low credit rating, controls on short-term inflows would prevent the country from borrowing abroad, because the low rating already minimizes the inflow of long-term funds. **Jeffrey Frankel** suggested that controls should be used cyclically and imposed only when a country is subject to massive inflows that do not appear consistent with the country's current macroeconomic conditions. The cyclical imposition of capital controls makes particular sense if one subscribes to the boom-and-bust view that investors' excessive optimism is followed by excessive pessimism. Frankel and **Robert Solomon** were also sympathetic with Cline's comment that the maturity-switching effect of capital controls is crucial to the architecture debate. Statistical studies of the leading indicators of currency crises show that the higher the percentage of capital inflow that is short-term, the higher the probability of a crisis. In addition, incentives for foreign direct investment address many of the moral hazard problems and lower the probability of a crisis. **Agustin Carstens** and **Pedro Pou** were instead of the opinion that the distinction between short-term and long-term investment is overstated because, in their experience, long-term investors are as light-footed as short-term investors.

In his reply, Edwards strongly disagreed with Cline's view that the ineffectiveness of capital controls at slowing down a real exchange rate

appreciation is inconsequential to the architecture debate. Real exchange rate appreciations always figure prominently in every post-mortem of recent crises. Finally, Edwards stressed that his analysis supports the sequencing argument that capital controls should be lifted last, but also raises concerns that the existence of controls might reduce a country's willingness to reform. Therefore, he favored having an explicit expiration date for the controls, to encourage countries to undertake the necessary steps to improve their regulatory and supervisory institutions.