BCC 11th Annual Conference: Uneven Growth Perspectives

Policy Panel 3 Capital Flows

A Few introductory remarks

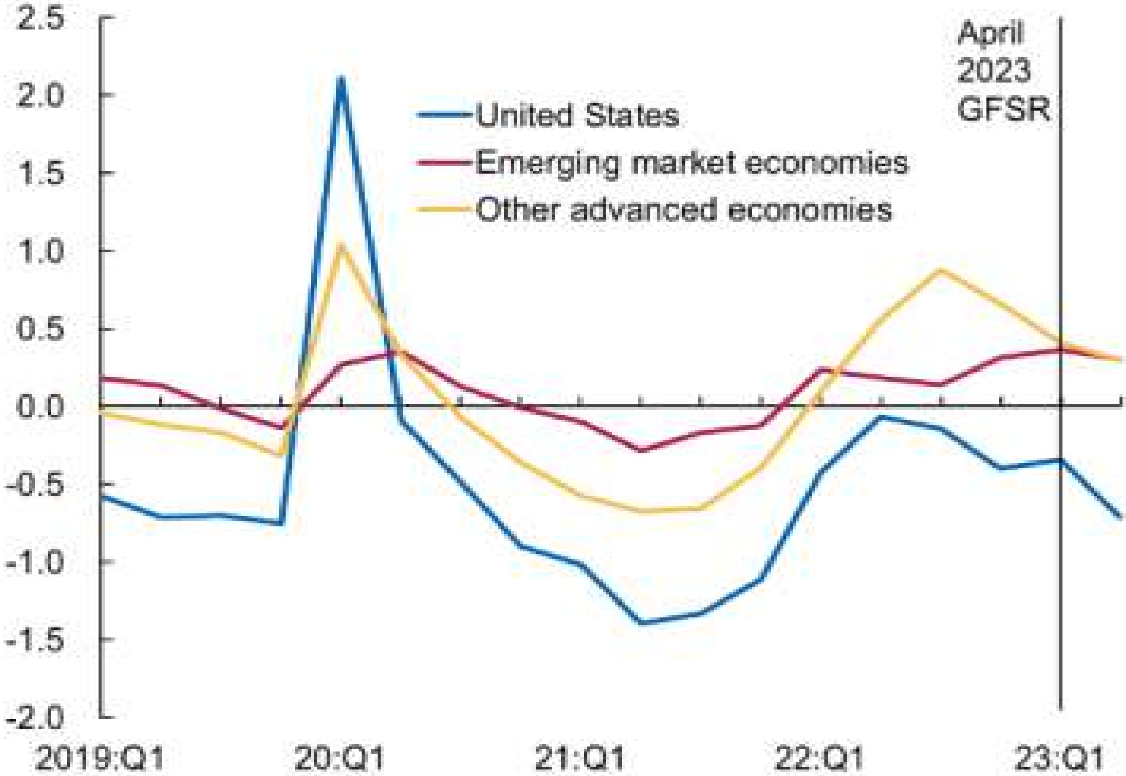
I welcome the participants to this third panel of capital flows, with a presentation by Professor Graciela Kaminsky of The George Washington University. Perhaps a few words on the last state of financial conditions in the world, as discussed in the last IMF World Economic Outlook and Global Financial Stability Report. As we know, capital flows are largely driven by interest rate differentials, and the monetary tightening in advanced countries, especially the USA, has driven up interest rates very rapidly, with an associated impact on US dollar appreciation. However, financial conditions, except very recently where financial markets have seen a correction, have remained quite loose. Nevertheless, we have seen capital outflows from emerging markets and deepened debt stress from many frontier markets.

From IMF July 2023 WEO and April 2023 GFSR

a) **Financial Market conditions**

Financial markets appear sanguine, and financial conditions have mostly continued to ease. Since the April 2023 *Global Financial Stability Report*, central banks have communicated that they could need to tighten monetary policy further. Even as yield curves remain inverted and recession concerns are prominent, financial conditions have mostly eased (Figure 1.1). A rally in the technology sector and higher equity prices, undoing some of the disinflationary impulses from tighter monetary policy, has supported this easing. In such circumstances, upside surprises to inflation could cause a sudden, sharp repricing of financial assets. The resulting tightening in global financial conditions could then interact with existing vulnerabilities in the financial system, which could amplify the tightening.

Figure 1.1. Financial Conditions Index
(Standard deviations from the mean)

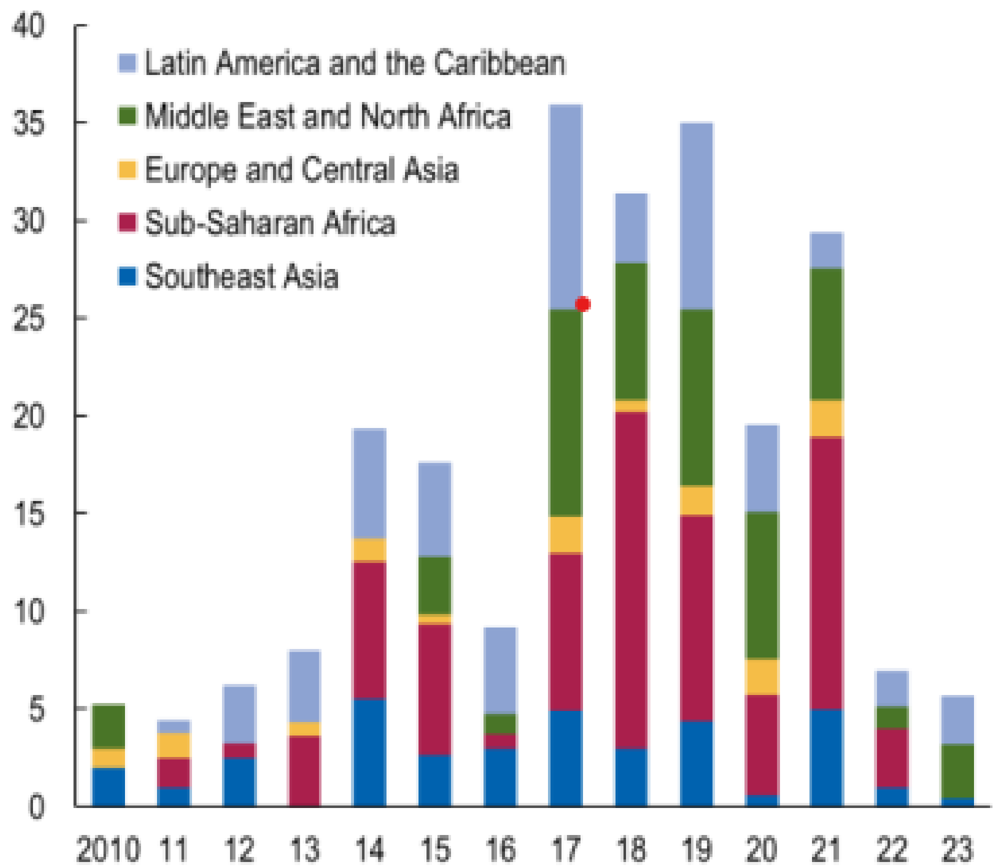


Sources: Bloomberg Finance L.P.; Haver Analytics; national data sources; and IMF staff calculations.

B) Sovereign Issuance and debt distress

Debt distress increases: Global financial conditions have generally eased since the March 2023 episode of banking stress (Box 1), but borrowing costs for emerging market and developing economies remain high, constraining room for priority spending and raising the risk of debt distress. **The share of emerging market and developing economies with sovereign credit spreads above 1,000 basis points remained at 25 percent as of June (compared with only 6.8 percent two years ago)**

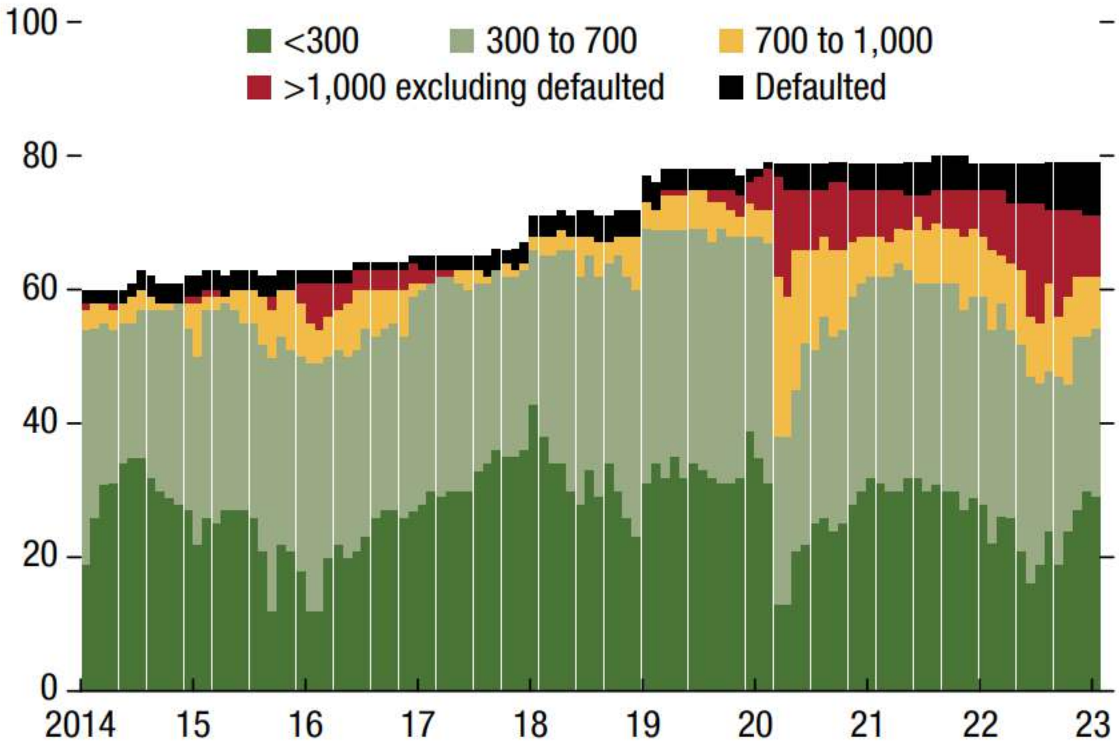
Figure 1.2. Frontier Sovereign Issuance by Region
(Billions of US dollars)



Sources: Bond Radar; and IMF staff calculations.
Note: The figure is based on 44 frontier economies defined as sovereigns in JP Morgan Next Generation Markets Index, plus any low-income countries that have issued eurobonds. Values for 2023 are year to date.

The number of distressed and defaulted sovereigns remains high compared with recent history.

3. Number of Sovereigns, by Spread

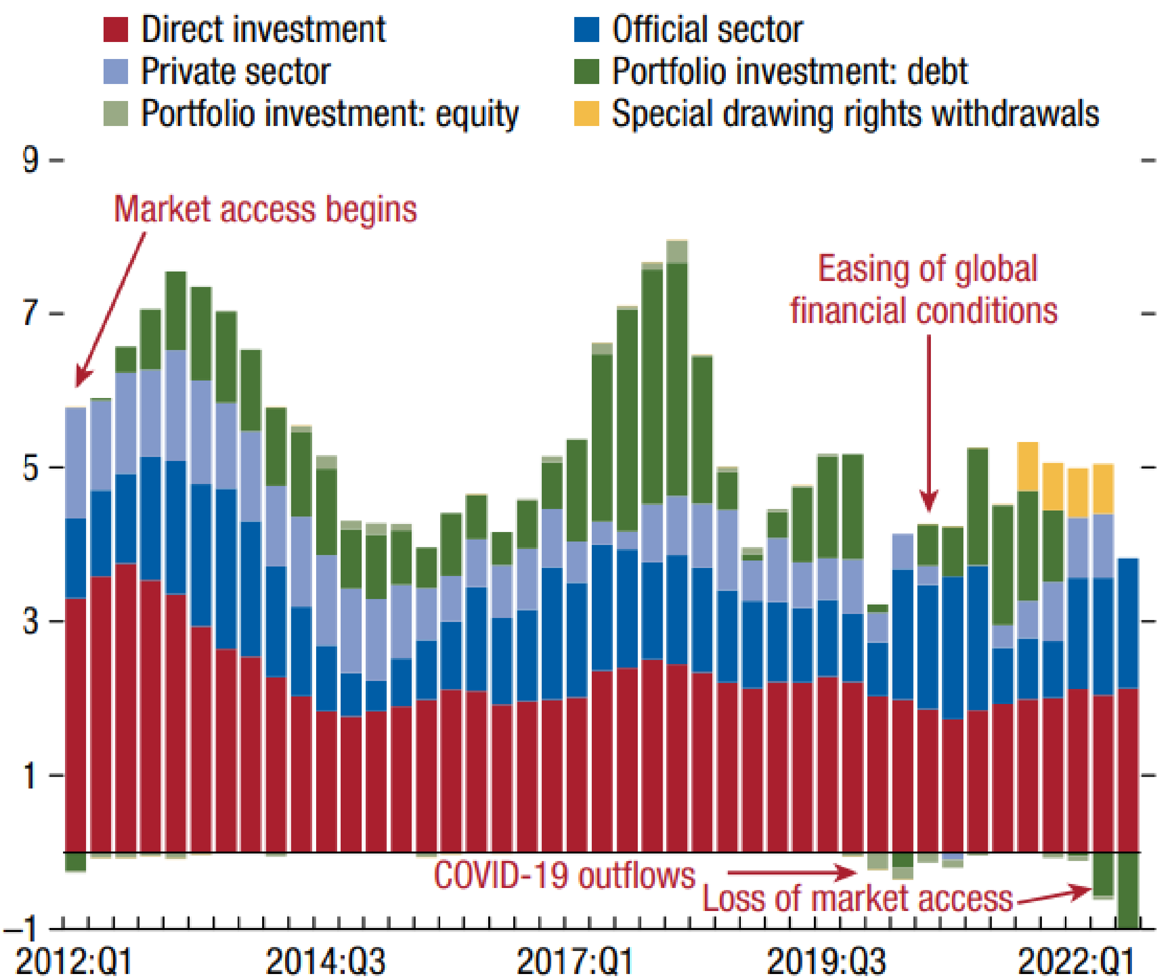


Sources: Bloomberg Finance L.P.; JPMorgan Chase & Co.; MSCI; and IMF staff calcul

C) Capital Flows breakdown

Figure ES.9. Frontier Market Nonresident Balance of Payment Capital Flows

(Four-quarter rolling sum to GDP)



Sources: Bloomberg Finance L.P.; Haver Analytics; IMF Balance of Payments data; and IMF staff calculations.