The Korea Institute of Finance (KIF) and the Thailand Fiscal Policy Research Institute (FPRI) have jointly prepared a report on “The Role of Regional Financial Safety Nets in Global Architecture.” In this report, they consider the role of global financial safety nets as a liquidity provision mechanism to prevent and resolve financial crises, and identify the position of regional financial safety nets in the global architecture. Then, they review operating mechanisms of existing regional financial safety nets and compare them with that of CMIM. Finally, they suggest policy recommendations for strengthening the CMIM function.

Despite rising concern that a large swing of cross-border capital flows may exert negative effects, there exists no international lender of last resort. In this regard, it is important to enhance the global financial safety nets which allow countries in need to have access to potentially substantial resources to prevent and reduce the costs of financial crises. Regional financing arrangements are positioned as a building block of global financial safety nets through which international cooperation is pursued to provide adequate liquidity so as to secure global financial stability.

Regional Financing Arrangements (RFAs) under consideration in the report include Medium Term Financial Assistance Mechanism in Europe (MTFA, also known as Balance-of-Payments Assistance), European Financial Stabilization Mechanism (EFSM), European Financial Stability Facility (EFSF), European Stability Mechanism (ESM), Arab Monetary Fund (AMF), Latin American Reserve Fund (FLAR), North America Framework Agreement (NAFA), and the Chiang Mai Initiative Multilateralization (CMIM).

The CMIM is the only RFA which has a clear link with the IMF lending. The CMIM’s strong link with the IMF program can delay quicker decision-making. Smaller sized RFAs can provide relatively quick assistance with limited conditions while larger sized RFAs necessitate an effective regional surveillance to mitigate the moral hazard problem. With regard to funding methods, real reserve pooling system provides more stable funding sources, a network of bilateral swap arrangements can leverage members’ reserves, and issuing bonds in the market may be cost-efficient but its condition can be affected by market sentiment. The CMIM has much to improve especially in terms of its analytical expertise. While the CMIM offers only one type of loan, other RFAs are equipped with various lending options depending on the type of problem.

Given these findings, the following factors should be considered in order to improve the effectiveness of the current CMIM: taking into consideration members’ risk characteristics and reserve availability in adjusting their contribution; enlarging the size of the CMIM; diversifying supporting schemes; encouraging voluntary bilateral swap agreements in the region as a complementary funding source; institutionalization; collaborating with the IMF
and other IFIs; and strengthening the regional surveillance system. In addition, the CMIM should introduce a crisis prevention function with diversified lending methods, sufficient size, and an advanced mechanism to analyze relevant information and provide a credible assessment of the potential risk factors.