

**WELCOME REMARKS BY
MR HOOKYU RHU
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AT THE OPENING CEREMONY OF THE
SEACEN HIGH-LEVEL SEMINAR ON
GLOBAL LIQUIDITY AND IMPACT OF CAPITAL FLOWS ON EXCHANGE RATES IN
EMERGING ASIA**

Bandung, Indonesia, 10 June 2014

Mr. Made Sadguna, Senior Director, Senior Advisor,
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Senior Officers from Bank Indonesia

Distinguished Resource Persons

Seminar Participants

Ladies and Gentlemen

Good morning,

It gives me great pleasure to extend to all of you a cordial welcome to the **SEACEN High-Level Seminar on Global Liquidity and Impact of Capital Flows on Exchange Rates in Emerging Asia** and to this beautiful city of Bandung.

Allow me to begin my Welcome Remarks by thanking our gracious host, the Bank Indonesia, for the excellent arrangements and warm hospitality in organising the Seminar. The SEACEN Centre is deeply grateful to Mr. Agus D.W Martowardojo, Governor, Bank Indonesia for hosting this event. I would also like to thank Dr. Hendar, Deputy Governor, Bank Indonesia for taking time from his busy schedule to deliver the Opening Address this morning.

We would like to take this opportunity to thank Dr. Masahiro Kawai, Former Dean of ADBI and Professor from Graduate School of Public Policy, University of Tokyo for the Keynote Address on “Asia’s Response to Capital Flows since the GFC”.

We also wish to thank the members of Organising Committee headed by Mr. Doni P. Joewono, Director, Head of Human Capital Development Group, Bank Indonesia, for their dedication and commitment in making this Seminar a success. Indeed, they have been working tirelessly in partnership with SEACEN many months prior to the Seminar to ensure that it is well planned and executed.

Ladies and Gentlemen,

Some signals are clear at present. There is now an expected recovery in the global economy, though it can be uneven. According to the IMF, global economy is forecast to grow by 3.6 percent in 2014 and 3.9 percent in 2015. During the past few years, capital flows issues have been placed at the top of their policy agenda at many forums for policy makers. Allow me to elaborate why.

Large inflows tend to complicate macroeconomic policy management resulting in excessive exchange rate appreciation, high sterilization cost, excess liquidity resulting in inflationary pressure and the risk of asset price bubbles as already experienced by some SEACEN member economies. Increasing share of volatile capital inflows, mainly portfolio investment and bank short-term financing raises the risk of their sudden reversal which may accompany adverse consequences.

Dear Delegates,

The uncertainty of QE tapering in the advanced countries has generated expectations concerning capital outflows and deepening of sell-off assets in the region. In fact, the Institute of International Finance (IIF), reported that in early 2013 emerging market conditions have continued to be quite choppy, including a significant market correction. However, retrenchment of flows in the middle of 2013 from the emerging economies is proven to be temporary as the global economy gained pace and the markets absorbed the impact of Fed tapering since its decision in December 2013. While the IIF continues to expect a gradual rebound in capital flows to emerging economies in 2014 and 2015, there are some elements of uncertainty, in particular when the advanced

economies start to increase their key interest rates, which may result in the narrowing of interest rate differentials, resulting in a surge of capital outflows from this region.

Hence, the challenge to policymakers in the developing economies is thus how to manage these boom-bust cycles of capital flows to ensure that they do not have any long-term adverse effect on the economic growth and financial stability. To address these issues, policy makers are implementing or searching for appropriate policy responses.

Among other things the two questions are attracting our keen attention. First, what are the right policy tools and the right combination of them to deal with large capital flows, both inflows and outflows at the individual economy level? Second, do we need regional initiatives or actions to complement and facilitate domestic policies in managing surge in capital flows? If yes, what are the more realistic regional initiatives or actions?

With regard to the first question, available policy tools to the authorities at the national level for managing capital flows could be grouped under five areas; exchange rate policy, monetary policy, fiscal policy, prudential rules and capital controls. In general, experiences have shown that it is more prudent to rely on some combination of these policy tools than to just rely on only one of them. SEACEN economies have been implementing different combinations of these policies including macro-prudential measures by taking into account country specific situations. However, the challenge is to find, for each case, the right combination of tools and the timing for implementation – I must state here, is not an easy task at all. In fact, Central Banks need to develop additional policy tools to deal with emerging challenges and problems.

With regard to the second question, the following factors indicate the necessity of regional cooperation and initiatives to complement domestic policies in managing large capital flows. Firstly, we know that any of these available policy tools or their combinations at the individual recipient economy level alone may not be adequate to deal with surge of capital flows as they involve significant costs or bring about other policy challenges. Moreover, some of these country level policies can have significant spill-over impact on neighbouring economies and hence, requiring regional attention.

Secondly, we need to reexamine both the strong “push” and “pull” factors. Hence, the more effective solution is to have some shared policy responsibilities i.e. by taking coordinated measures for both capital exporting economies and capital recipient economies to reap the full benefits of capital mobility. However, the challenge is to translate this into more consistent practice and it may not be realistic to expect such a global or even regional solution in the near future. Therefore, in the absence of any globally coordinated initiative, it is important for policy authorities and regional organizations in Asia to pay attention to strengthen and expand the regional cooperation and coordination in managing capital flows in order to support domestic policies.

Dear participants,

The SEACEN Centre is also grateful to Dr. Herbert Poenisch, SEACEN Consultant, in partnership with us in designing the programme and serving as a resource speaker; Other resource speakers which I would like to thank are:

- Dr. Rizki E. Wimanda, Senior Economist, Head of Research Specialist, Financial Market and External Sector, Economic and Monetary Policy Department, Bank Indonesia;
- Ms. Emily Poole, Manager, International Finance, Reserve Bank of Australia;
- Dr. Tu Yonghong, Professor, School of Finance, Renmin University of China;
- Dr. Kenneth Coates, University of Montevideo, Uruguay; and
- Dr. Ilhyock Shim, Senior Economist, BIS Asian Office

I also wish to thank, firstly my SEACEN colleagues for making this event a successful one and secondly to our member central banks for nominating all of you here for this Seminar. I am confident that this Seminar will be a highly engaging one of learning and sharing of experiences.

Lastly, let me conclude once again by thanking Mr. Agus D.W Martowardojo, Governor, Bank Indonesia for hosting this event. Also to Dr. Hendar, Deputy Governor, Bank Indonesia and all resource persons for the valuable contributions and support. I wish you a productive and rewarding learning experience and at the same time be able to find time to enjoy the culture and beauty of Bandung.

Thank you for your attention.