Capital flows less of an imminent threat to S'pore
Economists debate how Asia should respond to prospect of greater liquidity

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(SINGAPORE) The Republic faces less of an imminent threat from portfolio inflows than the rest of the region, agreed most participants at the Singapore Economic Roundtable (SER). But, there remained debate over how Asia's emerging economies should respond to the prospect of greater liquidity flowing into the region in search of higher returns.

Point of view: A participant questioned whether moves such as the property cooling measures are too reactive

The issues of capital flows to Asia, the effectiveness of policy responses and the need for greater global coordination dominated discussions at the SER, which was held on Nov 25.

The forum, organised by the Institute of Policy Studies, is held twice a year under Chatham House Rules, which forbid the identification of participants and their affiliations, to encourage freer discussion and debate. The 14th SER's focus on the impact of capital flows drew a larger than usual group of over 40 public and private sector economists.

Participants noted that although there has been a rebound in capital inflows into the region, these remain below the levels of 2007. 'Money is coming in, but I wouldn't say it's a wall yet,' one said.

For Singapore, although portfolio flows are large as a percentage of GDP, the openness of the economy and its position as a leading financial centre means that such flows do not have such a large impact as in some other countries. 'A lot of these flows come in, but then they go straight out', so net portfolio flows have generally been negative, said one participant.

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On policy measures needed, some were of the view that emerging economies should not rush to implement unconventional measures, such as capital controls, before exhausting such conventional ones as exchange rate appreciation.

One said that recent reserve accumulation in Asia suggested that there remains scope for countries to make further use of exchange rate appreciation.

Another participant pointed out however that most Asian economies do not view their exchange rates as undervalued or their reserves as excessive, but are experiencing overheating, which has prompted many, including Korea and Indonesia, to tackle capital flows with unconventional measures.

Most around the table agreed that macroprudential tools (such as tighter banking or financing regulations), when well targeted can be effective in stemming specific types of flows, as evidenced by Hong Kong and Singapore's moves to tackle frothiness in the property sector by, for example, raising downpayment requirements.

Interestingly, one participant highlighted that Singapore's property prices-to-rents ratios in the first half of 2010 were slightly above their long-run trend, which was not the case in China and Hong Kong. All three markets had seen a rapid appreciation in property prices from the trough of the recession.

Yet, another participant questioned whether moves such as the property cooling measures, are too reactive. Should policymakers not seek to pre-emptively discourage such sharp surges in inflows instead of reacting after they happen, he asked, triggering wider discussion on the need for global coordination of the monetary system.

The US Federal Reserve's policy of quantitative easing - which has expanded liquidity - has produced outsized effects on the global financial system, said one economist. He added that this has created problems for emerging economies and called for more policy coordination.

Another pointed out that such coordination is gradually getting under way, even as Asian central banks adopt more pragmatic ways to handle capital flows. 'Cooperation may be slow moving, but it is happening,' he said.

The morning's discussions followed presentations by the International Monetary Fund's resident representative Ravi Bala-krishnan on the issue of capital flows, as well as the Monetary Authority of Singapore lead economist Tu Suh Ping and Deutsche Bank chief economist and head of global markets research, Asia-Pacific, Michael Spencer.

The economists differed in their assessments of global uncertainties such as the health of the US economy and persistent debt woes in the eurozone, and what these mean for next year's economic outlook.

One participant argued that slow heating in the US economy, and evidence of a higher credit impulse, could possibly yield a good upside to global growth prospects, and hence Asia's too.