ASEAN WC-CAL Policy Note on
Capital Account Safeguard Measures: Recent Experiences

Introduction

In February 2019, the ASEAN Working Committee on Capital Account Liberalisation published the paper on Capital Account Safeguard Measures in the ASEAN Context (CAL Paper). The paper identified ASEAN's views and the different approaches and safeguard measures used in dealing with capital flows. It also served as platform for our engagement with third party institutions. Such a collective voice as a region as well as the consistent messages highlighted by our Governors at numerous events and on many occasions have gained traction, especially from major international financial institutions (IFIs) such as the International Monetary Fund (IMF) and the Bank for International Settlements (BIS).

More recently, IFIs have made commendable efforts in revisiting their policy thinking with progress on an integrated policy framework (IPF). The IMF, in particular, has demonstrated an openness and growing appreciation for a holistic approach to policymaking, taking into account all available tools to effectively manage challenging trade-offs. The IMF's work on the IPF recognizes the usefulness of combining conventional central bank policy tools with macroprudential policy measures (MPMs), capital flows management measures (CFMs) and foreign exchange intervention (FXI) in the face of volatile capital flows, especially if financial frictions are present. The IPF recognizes that these policy tools cannot indefinitely shield economies from necessary real economic adjustments, nor are they a substitute for well-functioning markets, healthy balance sheets and strong institutions. Indeed, efforts to deepen financial markets need to continue so as to improve market efficiency and allow countries to derive maximum benefits from these flows. However, judicious use of the appropriate policy tools can help mitigate financial stability risks associated with potentially volatile, short-term capital flows. The IPF also recognizes the role of precautionary CFMs in mitigating risks to financial stability and provides a framework for identifying the scenarios and conditions under which the use of CFMs may be appropriate. The IPF's findings are in line with recommendations of the recent IMF Independent Evaluation Office's (IEO) Review of IMF Advice on Capital Flows. Broadly speaking, these findings address and support some of the issues and concerns raised in the CAL paper.

Objectives and Key Messages of the Policy Note

This policy note is developed to serve the following objectives:

- Articulate ASEAN authorities' thoughts on the formulation of macroeconomic, financial, and capital flow measures as warranted by the circumstances to support price and financial stability.
- Supplement the IMF's work on the IPF which will provide crucial inputs to the IMF's review of its Institutional View on Liberalization and Management of Capital Flows (IV) in 2021. This note could also provide insights and guidance for the BIS-ACC's work on IPFs in emerging Asia.
- Provide updates on the actions taken by ASEAN authorities after the release of the CAL Paper in 2019, especially in the face of new challenges including the COVID-19 pandemic.

Three key policy planning parameters are deemed imperative for ASEAN authorities:

1. **Country authorities should be able to flexibly deploy a mix of policy measures (e.g. FXIs, CFMs and MPMs) as part of their overall policy response.**

   a) **Policymakers need the flexibility to consider all possible tools when designing the optimal policy mix for their country circumstances.** ASEAN countries are mostly small open economies and thus could be particularly susceptible to destabilizing pressures from cross border capital flows in search of yield, especially where capital flows are disproportionately large compared to the size of domestic financial markets. ASEAN countries should continue to deepen their financial markets to harness the benefits of capital flows. However, as part of this process, and taking into account their unique characteristics (i.e. policy framework, level of market development, financial frictions, etc.), ASEAN authorities should be able to deploy a combination of policy tools to mitigate risks associated with volatility of such flows. The optimal policy mix could be different from one country to another, depending on their country-specific characteristics[1]. This is supported by findings from an IMF study[2] which found that policy responses are highly heterogenous across countries even after controlling for the size of shock, and that the choice of policy tools deployed also varies depending on economies' structural characteristics such as the depth of the domestic FX market and balance sheet vulnerabilities.

   Actual conditions facing many ASEAN economies represent a departure from the assumptions of the Mundell-Fleming framework[3]. This is because, as rightly noted in the IMF's ongoing work on the IPF, having flexible exchange rates to absorb external shocks is only optimal in the absence of financial frictions. Where financial frictions exist, for instance where the FX market is shallow or when there are large destabilizing capital flows decoupled from economic fundamentals, flexible exchange rates may instead become an amplifier of shocks, and therefore other policy tools are needed to preserve stability.

   - Thailand's experience during the May-July 2019 period is a case where large portfolio inflows contributing to large, persistent one-sided exchange rate movements can reinforce adverse market dynamics through one-way bets and speculative trading behavior. The Bank of Thailand (BOT) has intervened in the foreign exchange market as deemed necessary to curb excessive exchange rate volatility, and deployed measures to disincentivize currency speculation, including by reducing the limit on the end-of-day outstanding balance in non-resident baht accounts. *See Annex for further details*

[1] Policy flexibility has been an important element of policymaking in ASEAN. In its review ("The ASEAN Way"), the IMF noted that "flexible inflation-targeting frameworks…have served the ASEAN-5 economies well in response to external shocks Not surprisingly, success—that is, positive outcomes—in most cases entailed significant changes to operating frameworks and refinement of policy objectives in response to challenges in the external environment. The ASEAN-5 economies' forward-looking monetary policy frameworks, active and independent liquidity management operations to align market conditions with the announced policy stance, and improved central bank transparency were important ingredients of their success". See "The ASEAN Way: Sustaining Growth and Stability" (2018).

[2] See "One Shock, Many Policy Responses." (2020)

[3] The framework states that countries with flexible exchange rates should allow these rates to adjust freely in response to shocks.

- The Philippine equities market has seen significant volatility at the onset of the COVID-19 pandemic. While the Philippine Stock Exchange (PSE) Index was within a tight band of 7,600 to 8,200 points in 2019, the early parts of 2020 showed a significant drop to 4,623 on March 19, a few days into the lockdown[4]. The portfolio investment account registered net outflows of USD 555 million in Q1 2020, a reversal from the USD 2 billion net inflows recorded in the same period in 2019[5]. Given that elevated capital outflows could lead to tighter liquidity and financial market disruptions as seen in previous financial crises, the BSP responded by using its full range of monetary and regulatory relief measures to ensure that the market remains liquid and to provide a revaluation boost against expected cash flows. These include, among others, (a) reduction of reserve requirements by 200 basis points which freed up PHP 200 billion in funds; (b) cumulative reduction of 200 bps in the policy rate to ease financing costs; (c) allowing banks to draw down from regulatory buffers (capital conservation, liquidity coverage, minimum liquidity ratios); (d) temporary relaxation of terms for BSP financing facilities; (e) time-bound relaxation of regulations on single borrowers limit and reserve requirements (e.g. allowing MSME loans to be considered as part of banks' compliance with reserve requirements); (g) four-week cancellation of the Term Deposit Facility auction and reducing volumes on auction offerings to discourage banks from recycling the liquidity back to central bank facilities; and (h) enabling operational relief measures for foreign exchange (FX) transactions to facilitate access to the banking system's FX resources for legitimate transactions. *See Annex for further details*
- Indonesia experienced high volatility and tightening liquidity due to uncertainties from the COVID-19 pandemic as well as uncertainties stemming from the US election, geopolitical tensions between China and the United States, China and India as well as in the UK. Such developments have eroded capital flows to and perpetuated currency pressures in emerging market economies including Indonesia. During 2020, Bank Indonesia has pursued various policy mixes to mitigate the risk of COVID-19 to the economy and promote the National Economic Recovery program. Bank Indonesia utilized the full range of policy instruments at its disposal in order to maintain stability of the rupiah exchange rate, control inflation, preserve financial system stability, and coordinated with the Government and Financial System Stability Committee in implementing other follow-up policies to maintain macroeconomic and financial system stability, while also supporting the national economic recovery. As part of BI's policy mix, Bank Indonesia has conducted Rupiah exchange rate stabilization policy through intervention in the spot market, Domestic Non-Deliverable Forward (DNDF), and purchases of Government Bond (SBN) from the secondary market. In 2020, six main policy aspects covered in BI's policy mix[6] include: (i) lowering BI 7-Day Reverse Repo Rate (BI7DRR), which has been cut five times (125 bps) in 2020 to 3.75%, the lowest level in history; (ii) stabilizing the exchange rate through the triple intervention mechanism in the spot market,

[4] See the Philippines Financial Stability Coordination Council's "2nd Semester 2020 Financial Stability Report"

[5] See BSP's "Report on Economic and Financial Developments First Quarter 2020"

[6] See BI's "Bank Indonesia's Annual Meeting: Synergize to Build Optimism for Economic Recovery" (2020)

Domestic Non-Deliverable Forward (DNDF), and purchases of Government Bond (SBN) from the secondary market; (iii) injecting large amounts of liquidity into banks to support the national economic recovery program, among others performed through monetary expansion and a reduction in the reserve requirement; (iv) relaxing macroprudential policies to boost credit expansion and finance the domestic economy as part of the accommodative policy, by maintaining a Countercyclical Buffer (CCB) ratio of 0%, a Macroprudential Intermediation Ratio (MIR) of 84-94% with a disincentive parameter of 0%, and a Macroprudential Liquidity Buffer (PLM) ratio of 6%, with a possibility to use as collateral for repo transaction with BI when banks are in need of additional liquidity, and a relaxation on the Loan to Value (LTV) ratio; (v) participating in the burden sharing scheme in the 2020 State Budget to support the national economic recovery program by BI's commitment to purchase SBN directly or from the primary market; (vi) accelerating the digitalization of payment systems as part of the fostering of the domestic economic recovery. *See Annex for further details*

The current crisis underscores the importance of countries' ability to flexibly calibrate the policy mix and deploy tools targeted at the source of risk as needed. Exhausting conventional measures before resorting to unconventional measures has become progressively less practical as global policy rates approach the effective lower bound. The current pandemic showed that many monetary authorities have expanded (and will continue to expand) their toolkits beyond the usual policy framework dealing not only with the shocks arising from the external and financial sectors but also those that are structural in nature (e.g. health and climate-related shocks) which have economic and financial implications. Any safeguard measure crafted by individual ASEAN member countries to manage the risks of capital flows amid the COVID-19 pandemic should be seen as part of a package of complementary policies to achieve multiple policy objectives in an unprecedented crisis.

Findings from empirical research are in line with the insights from country experiences. Capital flow measures have been found to be more effective in controlling capital flow volumes into EMEs with less developed financial markets (i.e. greater financial frictions), despite being ineffective in advanced economies with deep and open capital markets[7]. Studies using high frequency data show that a tightening in capital controls reduces financial vulnerability indicators such as bank leverage, bank credit, and exposure to portfolio liabilities, curtailing financial stability risks[8]. Some studies find that having flexibility to respond nimbly to circumstances matter. Ex-post CFMs – combined with FX intervention – can help stabilize exchange rate and interest rate movements in the event of shocks to cross-border capital flows, thereby avoiding costly disruptions to the domestic economy[9]. In addition, the flexibility to deploy a range of complementary policy tools is also helpful for reducing risks to the domestic economy.

[7] For example, see "Capital Controls: Gates versus Walls" (2012) and "The effectiveness of macroprudential policies and capital controls against volatile capital inflows" (2020)

[8] See "Capital-flow management measures: What are they good for?" (2015)

[9] See "Capital Flows and Foreign Exchange Intervention" (2019)

For example, in cases where domestic MPMs were used as complements to CFMs, there is also evidence that they have dampened private credit growth and housing price appreciation, thereby strengthening overall financial stability[10]. Empirical research has also found that MPMs that target foreign currency mismatches (e.g. restrictions on FX lending) are effective in reducing speculative (portfolio) capital inflows and linked to reduced probability of capital flows surges and banking crises over a three-year horizon[11].

b) **The likely persistence of international financial conditions conducive to large and volatile capital flows suggests a need for baseline policy toolkits to include measures that can be deployed pre-emptively.** Given the need for supportive fiscal and monetary policy over a sustained period in advanced economies, volatility in global capital flows is likely to be a structural feature in the international financial system, which could imply sustained pressures on EMEs, as opposed to short-term episodic events. Dealing with such persistent pressures may warrant the use of complementary policy measures, including MPMs and CFMs, as part of baseline policies – by having them in place for an extended period, rather than only temporarily when macroeconomic policy adjustment is constrained, or only after the risk of financial system instability has manifested as a result of external factors[12]. Pre-emptive and selective use of MPMs and CFMs during episodes of inflow surges can be useful for some countries in preventing buildup of domestic financial stability risks by targeting them at source, especially when other policy adjustments may be constrained or could take time to take effect (e.g. developing a deep and efficient FX market or encouraging widespread use of FX hedging). This may also be viewed in the context of building up buffers during good times – macroprudential, monetary or otherwise – to create policy space for adjustments during bad times.

   The literature suggests that the use of ex-ante CFMs or other policy tools (i.e. the ability to use them preemptively) to prevent the full absorption of capital inflows may be warranted from a prudential perspective. Ex-ante "against-the-wind intervention" by the central bank to prevent currency overvaluation in the first instance reduces the probability of a crisis[13]. In contrast, ex-post intervention to defend an overvalued currency raises the probability of a crisis. Countries that tightened restrictions on capital inflows prior to the global financial crisis (GFC) exhibited more resilience during the crisis, and countries that used some form of capital management measures immediately after the GFC experienced less overheating pressures in the post-crisis period. These

[10] See "How effective are macroprudential policies? An empirical investigation" (2018)

[11] See "The effectiveness of macroprudential policies and capital controls against volatile capital flows" (2020)

[12] Under the IMF's IV, CFMs can have a role in circumstances such as (1) When the room for adjusting macroeconomic policies is limited (i.e. economy is overheating, exchange rate is overvalued, further reserve accumulation is inappropriate or costly (2) When needed policy steps require time or when macroeconomic adjustments require time to take effect (3) When an inflow surge raises risks of financial system instability. See "The Liberalization and Management of Capital Flows: An Institutional View" (2012).

[13] See "Exchange Rate Management and Crisis Susceptibility: A Reassessment" (2014)

findings suggest that the counter-cyclical use of capital controls helps reduce boom-bust cycles in real output growth[14].

2. **Assessing the appropriateness of policy measures that may have implications on capital flows should take a holistic approach by considering the type of risk being targeted in the context of a country's overall policy settings, including to what extent similar measures are imposed on residents.** The basis of residency alone is too narrow for categorizing a measure as CFM or CFM/MPM. CFMs have been generally perceived as a strong policy response that should be used only sparingly and for a temporary period. Such an assessment, without considering the objectives and source of risk, may lead to a premature removal of policies. Historically, IFIs' views and advices on CFMs have tended to emphasize that they should be temporary, that they should not be used pre-emptively, and that they should be residency neutral. This stems from the thinking that CFMs, especially those that focus on outflows, tend to be deployed in order to support or prolong inconsistent macro policies. Given the potential for external shocks to spill over into the domestic economy via shifts in capital flows, some measures may inevitably need to target non-residents or FX transaction so as to address the source of risk and avoid creating inefficiencies in other sectors of the economy. While there may be costs from targeting non-residents/FX transactions, assessments of the appropriateness of policy measures need to balance these costs against that of inaction, i.e. the impact on risks to financial stability if no action is taken, or too late, which would not allow for buffers to be built up to mitigate the impact of external shocks. The mode of implementation of policies (i.e. their pre-emptiveness, permanence and differentiation by residency of capital) should be driven by the risks targeted by the policies. Moreover, labeling a measure as CFM without thoroughly considering its objectives and context could create an unnecessary and unwarranted stigma as investors, media and credit rating agencies are likely to focus on the restrictive measures and its near-term impact while ignoring the broader objective or longer-term benefits.

3. **IFIs have pivotal roles to play in advising sound policy responses among both AEs and EMEs, including through surveillance of the cross-border implications of domestic policy settings.** In a world where financial systems are increasingly interconnected and central banks are venturing into unprecedented monetary easing, the view that all will be optimal if each country keeps its own house in order is increasingly untenable. While recognizing the needs of AEs to pursue accommodative monetary policies, some small open economies could face stronger spillover effects through capital flows to domestic financial and economic conditions that could exacerbate existing vulnerabilities. The literature has highlighted the significance of spillovers from advanced economies'monetary policies into EMEs. EME central banks find their traditional monetary policy space eroded and financial stability threatened, and the impact of these spillovers can be magnified under floating exchange rate regimes[15]. Some of these countries could come under more pressure to utilize tools such as FXIs, MPMs, and CFMs, and thus EMEs will need sufficient degree of

[14] See "Managing Capital Inflows: What Tools to Use?" (2011); "Capital Controls: When and Why?" (2011); "Macroeconomic Effects of Capital Account Regulations" (2017)

[15] See "International channels of transmission of monetary policy and the Mundellian trilemma" (2016) and "US Monetary Policy and the Global Financial Cycle" (2020)

freedom in utilizing a mix of policy tools to respond adequately to external shocks. IFIs can assist EME policymakers through policy advice on seeking practical solutions that are grounded on an in-depth understanding of domestic financial structures and other specificities, and of both short-term and long-term challenges faced by the respective countries.

Conclusion

ASEAN authorities' use of the various policy tools to address challenges related to capital flows and exchange rate is aimed at preserving stability and facilitating orderly adjustment, and is not intended to substitute needed macroeconomic adjustments. The integrated policy approach provides ASEAN authorities the flexibility to utilize a wide variety of tools as necessary, but it does not ignore the need for macroeconomic adjustment and structural reforms which may be done concurrently and to be implemented for a longer period.

We hope that these points, along with our sharing of recent ASEAN experiences in employing a combination of policy tools to tackle the multi-faceted challenges highlighted in this policy note, could inform future work on integrated policy frameworks by the IMF and the BIS, and reviews of ASEAN countries' capital account liberalization and management. Our collective voice could pave the way for a greater recognition of the necessity to use CFMs in some circumstances and provide some level of comfort for ASEAN peers who are on their capital account liberalization journey.

Annex: Recent Experiences of ASEAN Member States in using Capital Account Safeguard Measures

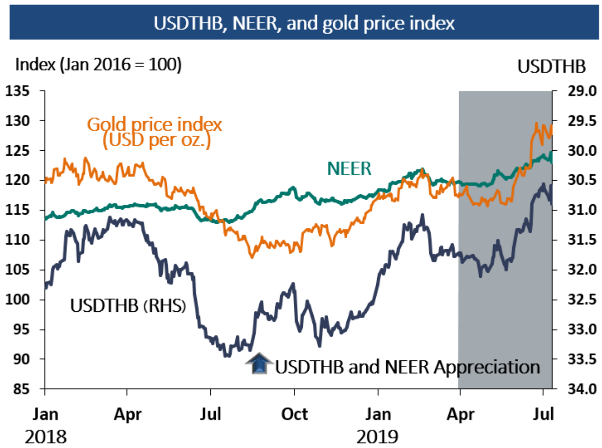
Thailand:

Addressing the impact of capital inflows and sharp Thai baht appreciation (May – July 2019)

Thailand's economic outlook in the latter half of 2019 was significantly affected by intensifying trade tensions between US and China. The resulting slowdown in global trade led to sharp decline in Thai exports which consequently affected employment and domestic demand. Against this background of slowing growth and rising uncertainties, the BOT's Monetary Policy Committee reversed its monetary policy normalization path and adopted a more accommodative monetary policy stance, cutting the policy rate by a cumulative 50bps by the end of 2019.

Shifts in global sentiment from a more dovish stance of major central banks also resulted in capital inflows to EMs including Thailand. These external factors combined with Thailand-specific factors contributed to a sharp appreciation of the Thai baht of about 3.5% against the US dollar between early-May to mid-July 2019 (Figure1).

Figure 1. The baht appreciated due to USD depreciation, net capital inflows, and higher gold prices.



Factors pressuring the baht

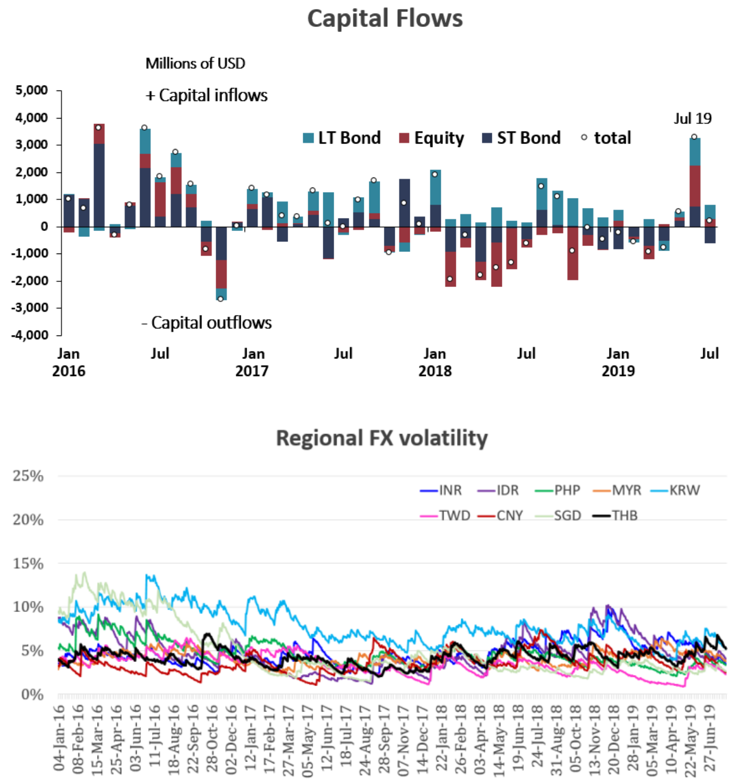
External factors
- USD depreciation from a more dovish Fed
- Dovish tilt by major central banks improved investor sentiment in Ems, including Thailand
- Higher gold prices prompting Thai residents to sell off gold holdings for profit-taking

Thailand-specific factors
- Sustained and substantial Current Account surplus
- THB's perceived safe-haven status due to Thailand's large CA surplus and international reserves
- Improved domestic sentiment post-election
- Increases weights of Thai assets in the MSCI and EMBI

Source: Bank of Thailand, Bloomberg and Reuters

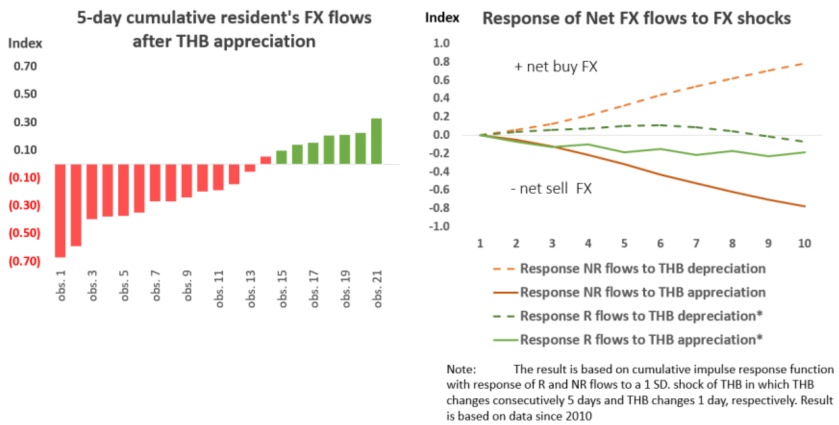
The BOT assessed that baht appreciation from capital inflows during this period could pose risks to stability and have negative macroeconomic repercussions. A closer look indicates that there were large capital inflows concentrated in some periods, including speculative flows into short-term bonds (Figure 2). Non-residents are also found to be large price influencers in the USDTHB market in some certain period. At the same time, residents can also amplify these effects induced by non-residents via a negative feedback loop whereby sudden THB appreciation caused by non-resident can trigger Thai enterprises, especially SMEs, to abruptly sell FX to cover their export proceeds (i.e. "snowballing behavior"), resulting in sharp one-sided movement and one-sided flows of the baht (Figure 3). Many Thai exporters are SMEs who are unhedged or do not have access to hedging instruments due to high costs or lack of knowledge (Figure 4).

Figure 2. **Capital flows and Regional FX volatility (2016 – July 2019); Net portfolio inflows concentrated in some periods lead to baht volatility**



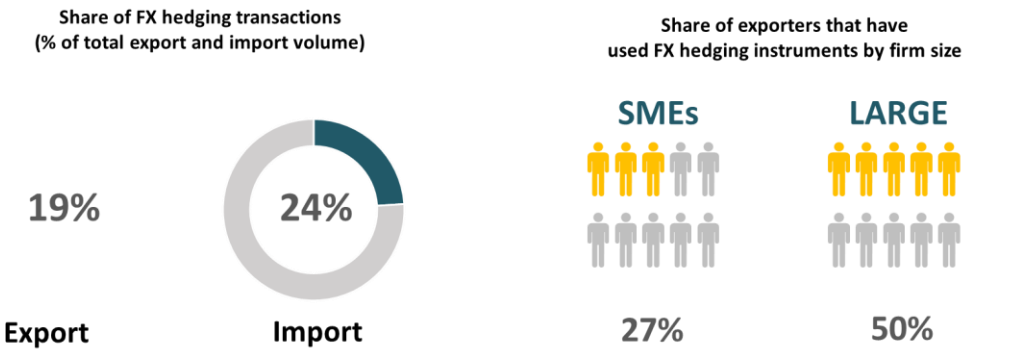
Source: Bank of Thailand

Figure 3. **Residents usually sell FX in a herd-like manner following persistent THB appreciation. NRs response to shocks in both directions in a momentum-following manner whereas residents tend to sell FX following appreciation shocks.**



Source: Bank of Thailand

Figure 4. Hedging is limited among Thai firms, especially SMEs.



Note: Figure is 5-year average from 2016 – 2020. For export, this is calculated from outstanding short position in FX forward contracts to total export value in the current month and previous 2 months. For import, this is calculated from outstanding long position in FX forward contracts to 3 months total import value in the current month and the next 2 months.

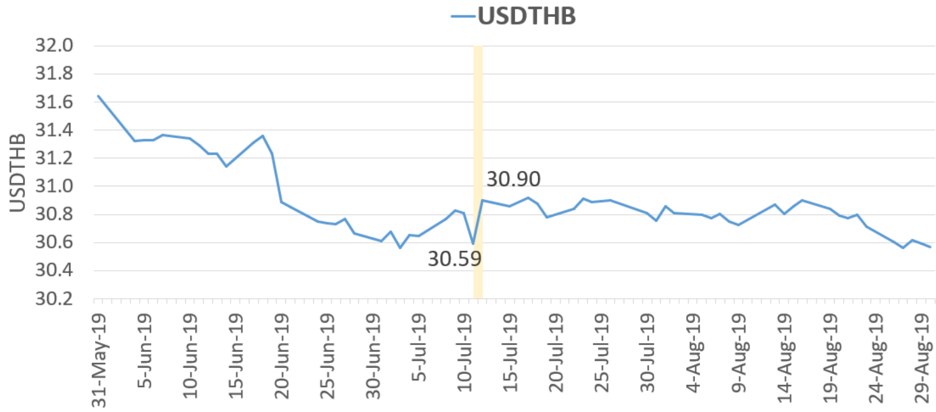
Remarks: Figure is cumulative from 2019 to Q3/2020. Calculated from the number of exporters that have previously used FX hedging instruments (short FX forward) to total number of exporters. Firm size is categorized by the company's income and the number of employees, which are calculated by the Bank of Thailand.

Source: Bank of Thailand and Thai Customs Department

To enhance surveillance of short-term capital flows and prevent Thai baht speculation by non-residents, the BOT announced several policy measures on 22 July 2019. First, the BOT tightened the reporting requirement for non-residents' holding of debt securities issued in Thailand whereby the full legal names of the ultimate beneficiary owner (UBO) must be reported by the custodian post-trade. This requirement is directly targeted at speculators who invested in short-term bonds and is unlikely to impose significant burden on legitimate investors. It is also an administrative measure adopted by many other countries such as South Korea and Malaysia. Second, the BOT reduced the limit on end-of-day outstanding balance of Non-resident Baht Accounts (NRBA) and Non-resident Baht Account for Securities (NRBS) from 300 to 200 million baht per non-resident. This measure aims to limit the channels for currency speculation and encourage non-residents to invest in more productive financial assets rather than idly placing their funds in these accounts for interest rate and exchange rate gains. Non-financial corporates with underlying trade and investment in Thailand remain able to request a waiver of this limit to be considered by the BOT on a case-by-case basis.

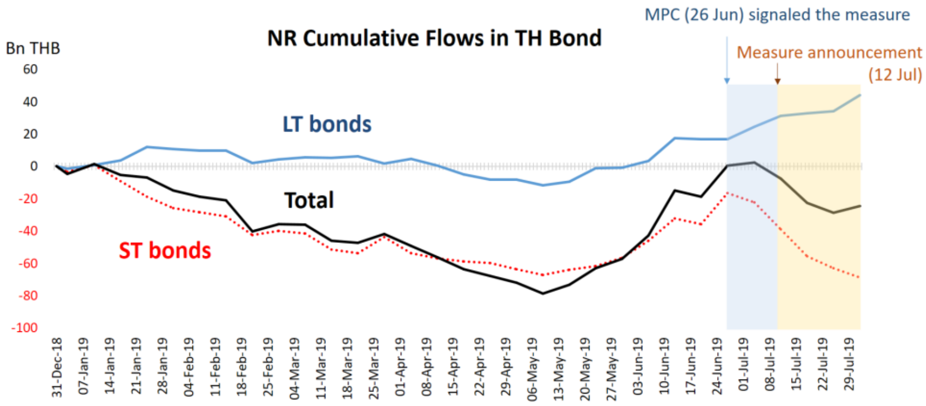
The NBRA/NRBS and UBO measures served their intended purpose of stabilizing the Thai baht, slowing down capital inflows, and curbing one-sided exchange rate expectation. After the measures announcement, USDTHB depreciated by approximately 1% from 30.59 (11 July 2019) to 30.90 (12 July 2019), and stabilized around the 30.80-30.90 range for about one month (Figure 5). Capital inflows into Thai government bonds also slowed down as non-residents started to sell off short-term bonds ever since the measures were first signaled in the MPC statement on June 26, 2019. The outstanding of NR holding on short-term government bonds decreased by 21.7% within two weeks from 111.5 billion baht (11 July 2019) to 87.3 billion baht (25 July 2019). Investments in long-term government bonds remain intact (Figure 6). While Investors and analysts viewed that the NRBA/NRBS and UBO measures were not radical, the measures did signal the BOT's preparedness to take additional actions as needed to the market. Such uncertainty helped curb one-sided expectation on THB appreciation, resulting in less speculative inflows.

Figure 5. USDTHB depreciated around 1% from 30.59 (11 June 2019) to 30.90 (12 June 2019). USDTHB was stable between 30.90 – 30.80 for around 1 month.



Source: Bank of Thailand

Figure 6. Investments in long-term government bonds remain intact.



Source: Bank of Thailand, Thai BMA

Further capital account liberalization and developing a new FX ecosystem (pre-2020 – 2021)

Amidst growing uncertainties and volatilities in the global financial market, the BOT recognizes the importance of building a financial ecosystem that could foster resilience against exchange rates and capital flows volatilities and to address structural problems in the foreign exchange market in a sustainable manner (Figure 7). Facilitating more balanced capital flows is among the key milestone towards resilience. In recent periods, Thailand's large and persistent current account surplus has led to constant capital inflows into the country. Against this backdrop, the BOT has provided greater convenience for residents' outflows, both in the form of outward direct investment and portfolio investment. The objective is to achieve better balance between capital inflows and outflows, and to increase opportunities for Thai investors to enhance returns and diversify risks. To this end, the BOT has been implementing a series of regulatory reform in accordance with the 2017 FX Regulations Reform roadmap as well the comprehensive FX Ecosystem Development Plan that was introduced under the BOT's strategic plan for 2020-2022. In addition, the BOT strives to ensure that Thai firms can manage exchange rate risks effectively and on a regular basis so that they are less vulnerable to exchange rate volatility. On 28 February 2020, the BOT increased the threshold of income and export proceeds that do not need to be repatriated[16]. This is to help businesses reduce fund transfer costs and better manage exchange risk risks, especially for exporters as the new threshold accounts for approximately 80 percent of all exports.

Figure 7. Developing a new FX Ecosystem in Thailand

Structural Problems in Thai FX market	Approaches
1. Thailand's low outward investment and persistent CA surplus (4% vs 8% of GDP for the past 5 years) leading to imbalanced capital flows.	**Facilitate investment in foreign assets for residents** **→ FX Investment Ecosystem** Encourage and facilitate a more balanced capital flows through outward direct investment and portfolio investment in foreign assets.
2. Thai firms have relatively low tolerance for exchange rate volatilities due to unfamiliarity with- and limited access to hedging instruments. Only 19% of total export volume are hedged by Thai firms and 24% for imports.	**Increase flexibility in FX risk management for firms** **→ FX Regulatory Framework** Relax FX regulations to create an environment that supports more balanced flows, provide more flexibility in FX risk management, and facilitate transactions process to enhance ease of doing business.
3. High cost of FX transactions. Exchange and Transfer fees in Thailand stood at 6.6% while those of others in the region stood at 2-4% total transactions value.	**Encourage competition among FX service providers** **→ Service Provider Landscape** Expand scope of activities and encourage new providers in order to enhance access for retail customers and help reduce cost of transactions.
4. Baht movement has been highly influenced by the offshore market. Substantial size of baht offshore markets passes along the volatilities from the global financial market to THB more easily. 85% of daily change in THB's movement is driven by foreign currencies movements.	**Enhance market intelligence and surveillance system by regulators** **→ Surveillance & Management** Encourage onshore transactions by non-residents and upgrade market surveillance system, which will allow bettering monitoring of investors' behavior, and thereby enable the timely implementation of targeted measures.

The COVID-19 pandemic took a heavy toll on Thailand's economic outlook as the country went into lockdown in March 2020. The Thai authorities have responded forcefully with extraordinary monetary and fiscal stimulus packages, utilizing the flexibility within their respective toolkits to create a policy mix that helped the Thai economy onto a path to recovery. On the monetary side, the BOT has cut its policy rate to a historical low of 0.50 percent and have stepped in to intervene in the FX market, provide USD liquidity and stabilize the bond market through bond purchases. In late 2020, the outcome of the US election and progress of the COVID-19 vaccine development strengthened confidence in the global economy and renewed capital inflows into emerging market

[16] See BOT Press Release No. 11/2020 "Increase of repatriation threshold to 1 million US dollars" (28 February 2020)

economies including Thailand. Concerned that rapid appreciation of the Thai baht could affect the fragile economy recovery, the BOT rolled out a set new measures in November 2020[17] to mitigate exchange market pressure and address structural impediments in the Thai FX market, accelerating progress towards the new Thai FX ecosystem:

i. Allowing Thai residents to freely deposit funds in foreign currency deposit (FCD) accounts and allowing free fund transfer between resident's FCD accounts which will enable exporters to effectively manage liquidity and FX risks, and allowing FCD transactions to be conducted electronically to reduce transaction costs.

ii. Increasing limits on investment in foreign securities and expanding the universe of eligible financial products to enhance Thai residents' portfolio diversification.

iii. Requirement for investors to complete pre-trade registration process before investing in Thai debt securities. This builds upon the UBO reporting requirements to enhance monitoring of non-resident investors' behavior and would enable timelier implementation of targeted measures if needed.

To cope with the impact of continued capital inflows and pave the way towards the new FX ecosystem, the BOT announced on 5 January 2021 further relaxation of foreign exchange regulations under the Non-resident Qualified Company (NRQC) Scheme[18] to allow greater flexibility to conduct foreign exchange transactions against the baht with domestic financial institutions. This includes removing requirement for proof of underlying trade and investment for each transaction and allowing anticipatory as well as balance sheet hedging.

[17] See BOT Press Release No. 81/2020. "BOT accelerates measures to advance the development of the new Thai FX Ecosystem" (20 November 2020)

[18] See BOT Press Release No. 1/2021. "Relaxation of Foreign Exchange Regulations Under the Non-resident Qualified Company Scheme (NRQC Scheme)" (5 January 2021)

Philippines:

As a small open economy, the Philippines is prone to significant capital inflows and sudden reversals, which could cause large fluctuations in the exchange rate and bring about possible destabilizing effects on the domestic economy. The dynamics in capital flows and exchange rate in the Philippines have been driven by both cyclical and structural factors. The accommodative monetary policies in major advanced economies post-GFC have been a major cyclical factor behind capital inflows into emerging economies, including the Philippines, as investors have been encouraged to seek higher-yielding assets. Stronger economic growth in emerging economies relative to advance economies have also played a role. The confluence of structural factors, including international regulatory reforms and domestic developments and regulatory initiatives, have likewise contributed to the dynamics of capital flows and exchange rate in the Philippine economy.[19] To deal with these fluctuations in capital, the BSP utilizes an expanded policy toolkit which includes the following: flexible inflation targeting; flexible exchanges rates; maintenance of adequate international reserves, FXIs, CFMs, and macroprudential measures[20]. The country's flexible exchange rate generally works as a shock absorber, that the BSP's initial response in cases of exchange rate pressures is to allow the exchange rate to adjust accordingly. Buffers built into the economy against external shocks also allow the BSP to avoid reacting aggressively to exchange rate developments. Although the BSP adheres to flexible exchange rate policy, it still participates in the FX market to smoothen volatilities that threaten its inflation target. CFMs, similar to FXIs, are considered as a last line of defence due to their many potential unintended effects.

Exchange rate and capital flows are also incorporated in models and macro-surveillance tools used for policy analysis as they can have significant implications on both price and financial stability, including the orderly functioning of markets. Consideration of FX and capital flow movements allows the BSP to respond to their consequences with the appropriate tool. In particular, the BSP gives attention to excessive FX volatilities as these could exacerbate vulnerabilities in the financial market especially when firms are heavily exposed to FX-denominated liabilities. Financial variables like market interest rates and stock market returns are typically the most sensitive to capital flow and exchange rate movements.[21] The BSP diligently monitors the financial market with particular focus on excessive volatile movements of asset prices. To reduce pressures on financial stability, the BSP implemented fine-tuning measures to gain greater flexibility in the conduct of monetary policy (MP) operations and to ensure adequate liquidity to support economic activity. The BSP refined its MP

[19] For instance, from 2007 to 2019, the BSP has implemented a series of FX liberalization measures to make FX regulations responsive to the changing needs of the economy and to support the government's thrust towards greater openness with the country's increasing integration with global markets. The liberalization of FX rules has facilitated the flow of greater cross-border investments and supported the deepening of the domestic capital market. The first investment grade rating of the Philippines in 2013 and the succeeding upgrades, as well as the further liberalization of foreign bank entry in 2014 have also supported the inflow of foreign investments. The BSP's adoption of the Basel III Accord for universal and commercial banks in the Philippines starting in 2014 could have also played a role.

[20] Examples of MPMs in the Philippines are caps on non-deliverable forward (NDF) transactions, limits on banks' foreign exchange net open positions, as well as the conduct of real estate stress tests (REST). These MPMs are geared primarily to influence the credit cycle, to limit the build-up of system-wide risks, and to alter the incentives of market players.

[21] The exchange rate can affect the economy through three main channels. First, exchange rate pass-through to inflation: exchange rate swings directly impact domestic inflation through their effect on import prices. Second, export competitiveness: a stronger domestic currency is generally associated with weaker exports, lower firm profits and slower growth. And third, domestic financial conditions are affected by a set of 'financial' channels, the direction and size of which reflect balance sheet compositions and the responsiveness of capital flows. Market expectations on the direction and volatility of capital flows and exchange rates may have an important role to play.

framework by adopting an interest rate corridor (IRC) system in June 2016. The IRC has improved monetary transmission as monetary policy now has greater traction in influencing market rates.

It is important to highlight that the expanded toolkit also includes the prudent regulatory framework over banks, the close coordination with fiscal authorities, and the clear and timely communication of policy measures. The BSP calibrates this policy mix based on the strength and persistence of the shock, threat to the inflation target and financial stability, state of the economy, and the efficiency of the measures.

2019

In 2019, financial markets in ASEAN were calmer when the US Fed shifted to a dovish tone and member economies addressed country-specific issues. For the Philippines, in particular, signs of receding inflationary pressures supported the improved investor sentiment during the period[22]. The financial account recorded lower net inflows of USD 7.3 billion from USD 9.3 billion in 2018. This emanated from the large drop in net inflows in other investment and direct investment accounts, which tempered the reversal to net inflows of the portfolio investment account.

Policy rate adjustments. In 2019, the BSP reduced its key policy interest rate by 25 bps each, bringing the rate for the overnight reverse repurchase or RRP facility to 4.0 percent. The interest rates on the overnight lending and deposit facilities were likewise decreased accordingly. This brought the cumulative policy rate cut to 75 bps during the year. In deciding to reduce the key policy interest rate in 2019, the BSP noted that price pressures have continued to ease and inflation expectations also remained well anchored to the inflation target range based on the BSP's survey of private sector economists. The policy rate cuts considered the impact of the budget impasse on the economy at the early part of the year as well as deteriorating external growth prospects. Upside risks to inflation over the near term emanated mainly from the volatility in oil prices due to geopolitical tensions in the Middle East and from the potential impact of the African swine fever outbreak on food prices.

Reduction of Reserve Requirement Ratio (RRR). The RRR was successively reduced from 18 percent to 14 percent in June, July and December 2019. The RR cuts were in line with the BSP's broad financial sector reform agenda to promote a more efficient financial system by lowering financial intermediation costs. At the same time, the adjustment in RR ratios is aimed at increasing domestic liquidity in support of credit activity.

Capital market reforms. In December 2019, the SEC approved the guidelines prepared by the Capital Markets Integrity Corp. (CMIC) on securities borrowing and lending (SBL) and short selling. CMIC's guidelines were made to address the effect of SBL and short selling on trading participants' books and records, error transactions and any effect on the risk-based capital adequacy (RBCA) ratio of trading participants. These guidelines: (a) limit short selling transactions to "eligible securities" or those that are owned by companies in the PSE index (PSEi); (b) require trading participants to ensure that all involved parties in a short sale transaction have the necessary borrowing arrangements prior to any deal; and (c) require that all lending securities are registered with the SEC and have a Securities Lending Authorization Agreement, and that borrowing parties have a Master Securities Lending Agreement before any transaction.

[22] See Asian Development Bank "Emerging East Asian Local Currency Bond Market: A Regional Update" (2019)

Foreign exchange (FX) market reforms. Since 2007, the BSP has been introducing waves of FX regulatory reforms to address the dynamic needs of the Philippine economy given the evolving interconnection of global markets. The reforms have been aligned with the BSP's thrust to further deepen and develop a robust capital market through a more liberal policy environment, taking into consideration adherence to international practices and standards. In March 2019, the BSP released its 11th wave of FX liberalization reform targeted mostly to both inward and outward foreign investments. The reforms intend to facilitate access to the banking system's FX resources for legitimate transactions, and further streamline and simplify procedures and documentary requirements for FX transactions.

2020

In early 2020, as lockdowns were enforced to contain the spread of the COVID-19 pandemic, EMEs experienced a massive outflow of portfolio funds with levels surpassing the reversals recorded during the GFC (based on Institute of International Finance Report) [23]. Investors shifted towards safe-haven and liquid assets given the uncertainty brought about by the health crisis[24]. As such and similar to other EME markets, the Philippines domestic financial market experienced a period of stress with equity sell-off[25] and heightened risk premia[26]. Nonetheless, it is notable that the Philippine peso remained relatively stable compared to currencies in the region during this turbulent period[27]. Equities subsequently recovered while bond yields remained low as markets stabilized. The timely and decisive policy measures undertaken by the BSP to provide liquidity in the secondary bond market helped calm markets and lent much needed support to the domestic economy.

Policy rate adjustments. The BSP took decisive policy measures to support domestic liquidity in the midst of the pandemic. The cumulative 200 bps cut in the policy rate was complemented by liquidity-enhancing measures and regulatory relief to banks' borrowers experiencing financial difficulty amid the implementation of lockdown protocols. Rate cuts in 2020 brought the RRP rate to the current 2.0 percent. Amid a within-target inflation outlook, the BSP undertook a series of policy rate reductions to provide support to domestic activity and market sentiment amid the impact of the COVID-19 pandemic on the economy.

Reduction on RRR. The 200-bps reduction in the RRRs (from 14 percent to 12 percent) of universal and commercial banks was intended to help alleviate the liquidity strain on banks arising from the COVID-19 pandemic and ensure sufficient liquidity in the banking system to accommodate the funding needs of both the retail and corporate sectors in support of economic activity. Furthermore, the RRRs imposed on thrift banks and rural banks were reduced by 100 bps, which is expected to increase the lending capacity of these banks to support the financing needs of micro, small, and medium enterprises (MSMEs) as well as rural community-based clients. At the same time,

[23] See IIF report "Capital Flows Report: Sudden Stop in Emerging Markets" (2020)

[24] See CNBC article "Gold surges to 7-year top as pandemic fears spark safe-haven rush" (24 February 2020)

[25] See Business Inquirer article "Stocks slide on COVID-19 fears" (10 March 2020)

[26] The financial account recorded net outflows of USD3.9 billion in the first nine months of 2020, a turnaround from net inflows of USD5.1 billion in the same period in 2019. The shift to net outflows was accounted for by the reversal in portfolio investment account to net outflows of USD4.3 billion for the period January-September 2020 from net inflows of USD4.4 billion for the same period in 2019. Furthermore, there was an increase in net outflows of other investments to USD2.5 billion, from the USD2 billion recorded in January-September 2019. Unconventional monetary policy 7 billion.

[27] See Business Mirror article "Peso remains stable amid COVID-19 fallout" (10 July 2020)

the BSP allowed newly granted loans to MSMEs and newly granted loans to large enterprises[28] as alternative compliance with RRs until 29 December 2022. These measures were aimed to further reduce the financial burden on loans to enterprises to ensure adequate liquidity in the financial system and help reduce borrowing costs. A cap on the aggregate loans to MSMEs and LEs utilized under this relief measure was set to ensure that banks still have sufficient amount of deposits on hand to cover possible withdrawals. A review of the policy will be done at the end of 2022 to ensure the policy intent remains relevant[29].

Capital market reforms. In January 2020, the Securities and Exchange Commission issued the a revised implementing rules and regulation (IRR) of Real Estate Investment Trust (REIT) Act of 2009 which provides, among others, the minimum public ownership requirement of a REIT and the condition that whatever capital is raised through a REIT in the Philippines will be reinvested requirement for reinvestment in the country capital raised through a REIT[30]. The SEC also approved new rules requiring companies that plan to conduct an initial public offering to have a minimum public float of 20 percent to 33 percent, depending on market capitalization in August 2020[31]. The establishment of REIT market provides foreign investors an added opportunity to diversify their investments in the Philippines.

FX market reforms. In light of the COVID-19 pandemic, the BSP granted operational relief measures for FX transactions to facilitate the public's access to FX resources of the banking system to finance legitimate FX transactions such as easing of documentary requirements in reporting FX transactions with the BSP and waiving of specific FX-related fees, among others.

[28] A large enterprise refers to a sole proprietorship, partnership, corporation, or cooperative that: (1) does not belong to a conglomerate structure, (2) has an asset size (less land) of more than PHP 100 million with an employment size of 200 employees or more, and (3) has been directly and adversely impacted by the COVID-19 pandemic.

[29] See BSP Circular No. 1100 series of 2020 "BSP Announces Limits on Loans to MSMEs and Large Enterprises Used as Alternative Compliance with Reserve Requirements" (11 December 2020)

[30] Key provisions in the Revised REIT IRR include, among others: (a) The minimum public ownership requirement (MPO) of a REIT has now been reduced to at least one-third (1/3) of the outstanding capital of the REIT, with at least 1,000 public shareholders each owning at least 50 shares; and (b) Reinvestment in the Philippines is now required for any sponsor or promoter who contributes income-generating Real Estate to a REIT. This requirement is intended to ensure that whatever capital is raised through a REIT in the Philippines will be reinvested in the country. The Ayala REIT (AREIT) Inc. was the first company in the Philippines that listed in the brand-new asset class at the PSE in August 2020.

[31] Under the approved guidelines, a company with market capitalization of PHP 500 million should offer at least 33 percent of the outstanding capital stock to the public, while a firm with over PHP 500 million up to PHP 1 billion market capitalization should sell at least 25 percent of the outstanding capital stock. A company with market capitalization of more than PHP 1 billion should offer a minimum public float of 20 percent. A company listing through an IPO must also maintain a public ownership of at least 20 percent at all times. A company that plans to list with the Philippine Stock Exchange by way of introduction or with no public offering is also required to have at least a 20-percent public float upon and after listing. A company that is doing a backdoor listing is required to have at least a 20-percent public float upon and after listing.

Malaysia

BNM's objective in managing external financial shocks is to ensure orderly market adjustments. This is consistent with the monetary policy framework[32], whereby adjustments in the domestic financial markets are necessary to cushion the impact of such shocks to the domestic economy. Congruent to this, the development and depth of the domestic markets is an important prerequisite for the adjustments to take place in a non-destabilising manner. Nonetheless, given our financial integration with global markets, Malaysia remains susceptible to large movements in capital flows due to the inherent risk premia attached to emerging market economies (EMEs). As such, while the flexibility in the exchange rate remains our first line of defence to manage external shocks, the utilisation of an expanded toolkit may be necessary from time to time to address specific risks. These policy tools include targeted foreign exchange intervention (FXI), macroprudential measures (MPMs) and capital flow management measures (CFMs). In short, BNM's optimal configuration of policies is determined by the assessment of risks that need to be addressed and constraints within the operating environment.

This flexible approach in policymaking has continued to serve the Malaysian economy well by successfully safeguarding the stability of the Malaysian economy and the financial system. At the height of financial market stress in March 2020 as the COVID-19 crisis was unfolding, Malaysia experienced sharp portfolio outflows amid heightened investor risk aversion, in line with other emerging market economies. During the first quarter of 2020, Malaysia experienced non-resident portfolio outflows amounting to USD 6.3 billion. As a result, the ringgit exchange rate depreciated by 4.9% against the USD to close at 4.3025 (end-Dec 2019: 4.0925), and the one-month onshore implied volatility for the exchange rate spiked to 7.55% (end-Dec 2019: 3.52%). Policy flexibility was very crucial in managing the stress from capital flow reversals. With various policy tools in hand, exchange rate flexibility remained the first line of defence against external shocks during this period. However, as excessive ringgit movements could be destabilising and may in itself be a source of additional shocks[33], targeted foreign exchange intervention (FXI) was also used to mitigate excessive exchange rate volatility and provide sufficient foreign exchange (FX) liquidity to the markets to maintain orderly market conditions (see *Chart 1*).

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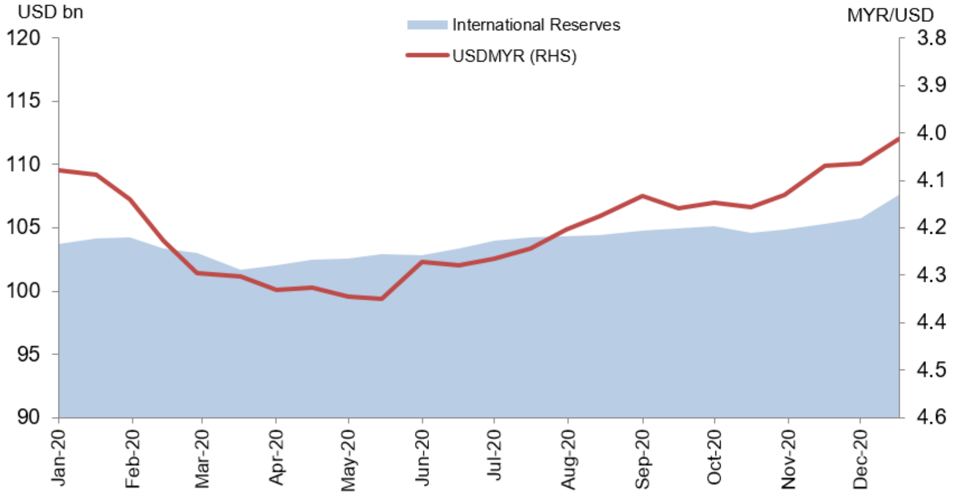
[32] BNM formulates and conducts monetary policy to keep inflation low and stable, while ensuring that it is supportive of sustainable economic growth. Malaysia also maintains a flexible exchange rate regime.

[33] For instance, the financial channel of the exchange rate could amplify the shock in exchange rate movements by influencing the supply and cost of foreign currency funding through banks' and firms' balance sheet capacity, with potential implications on domestic economic activity. A depreciation of the domestic currency would weaken domestic borrowers' balance sheet capacity, and subsequently their creditworthiness, thereby reducing risk-taking and lending / borrowing activities. Source: "Does the financial channel of exchange rates offset the trade channel" (2016)

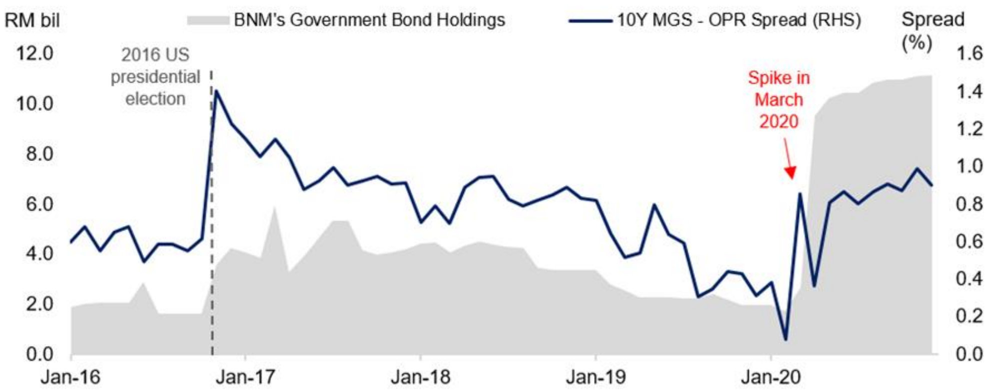
Chart 1: BNM International Reserves Level and Exchange Rate Movements against the US Dollar



*The period of change in reserves may not correspond to the turning point of ringgit
Source: Bank Negara Malaysia

In the domestic government bond market, the portfolio outflow pressures were further amplified by the impact of exchange rate depreciation on non-resident investors' bond returns. Against this backdrop, it was crucial to ensure that financial intermediation remain intact. To facilitate orderly price adjustments in the domestic bond market, the Bank increased its outright purchase of Government securities by RM9.4 billion (March to December 2020) as part of its open market operations. These purchases provided sufficient liquidity in the market (see *Chart 2*). Consequently, as global market stresses began to abate from April 2020 onwards amid large scale liquidity injections and low-for-long monetary policy commitments by major central banks, global investor sentiments recovered gradually, leading to the improvements in domestic financial market conditions, which were supportive of the economic recovery.

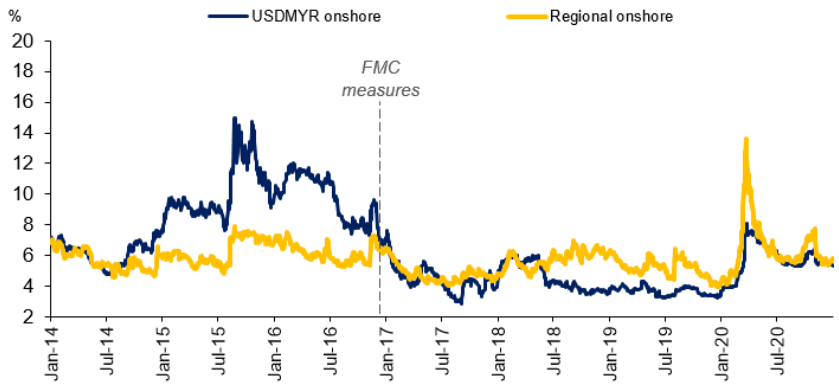
Chart 2: BNM's Government Bond Holdings & 10-Year Malaysian Government Securities (MGS) – Overnight Policy Rate (OPR) Spread



Source: Bank Negara Malaysia

While these policy tools were effective in ensuring orderly market adjustments, it is worth noting that existing financial market measures have also provided a stronger footing for domestic markets to absorb shocks in capital flows arising from global spillovers during this period. For instance, the series of measures introduced by the Financial Markets Committee (FMC) from 2016 to 2017[34], have deepened and improved the functioning of the onshore financial market by providing both residents and non-residents better access to the onshore market. Consequently, throughout 2020, adjustments in the domestic financial markets were relatively less abrupt (see *Chart 3*). This helped to ensure that broader financial intermediation remained intact, which helped in avoiding further adverse implications to the real economy. In recognising the need for market participants and businesses to better manage their FX risks in an environment of heightened uncertainties, additional hedging instruments and flexibilities, as well as several new measures[35] were implemented in 2020 which also enhances overall functioning and efficiency of the domestic FX market. Together, these measures have helped to bolster the exchange rate's role as a shock absorber.

Chart 3: Onshore Implied Volatility: Ringgit and Regional Currencies against the US Dollar



*Regional countries: Indonesia, Philippines, Singapore, South Korea, Taiwan and Thailand
Source: Bloomberg

Moving forward, as the global economy recovers with the normalisation of economic activities following the rollout of vaccine programmes, the inevitable unwinding of ultra-accommodative global monetary policy would need to occur at some point. When this happens, EMEs should expect reversals of flows and adjustments in the domestic financial markets. This would require EMEs to have the access and flexibility to an expanded policy toolkit to manage these volatile capital flows. To sum up, the strategic management of capital flows, financial market adjustments and its implications to the economy must be pragmatic and be allowed to evolve across time. When the risks seen in financial markets have abated and when market conditions allow, countries should gradually unwind these policies and undertake the necessary structural reforms to further enhance market openness, including the longer-term capital account liberalisation agenda.

[34] Please refer to "Capital Account Safeguard Measures in the ASEAN Context" (2019)

[35] Resident exporters are exempted to convert export proceeds below RM 200,000 per transaction into ringgit; residents are free to hedge foreign currency loan obligations up to the duration of underlying tenure; residents and non-residents are free to unwind their hedging for any underlying except portfolio investment; residents are free to obtain financial guarantee from non-residents; residents are free to issue financial guarantee to non-residents with some exceptions.

Indonesia

To deal with the volatility of capital flows, Bank Indonesia has implemented a set of policy mix, in particular since the global financial crisis, when flows driven by vast global excess liquidity from ultra-quantitative monetary easing and near zero interest rates in advanced economies were seeking for high returns. The policy framework was established based on inflation targeting, using the interest rate as the main instrument, complemented by exchange rate policy, macroprudential measures and capital flows management (CFM), which based on historical experience, has proven to be an effective formula in achieving Indonesia's economic resilience. In particular, CFM is conducted to support the exchange rate policy, especially during surge period of capital inflows and heightened risks of capital reversals. Bank Indonesia has clearly stated that CFM implementation in Indonesia is to complement, not substitute, the sound monetary policy[36]. Three main CFM principles implemented in Indonesia includes: (i) the measures are used to mitigate the undesirable impacts of capital flows volatility to exchange rates instability, as well as to monetary and financial system; (ii) the measures target the short-term and speculative capital flows; and (iii) the measures are consistent with the broad principle of maintaining the free foreign exchange system.

Indonesia's experience in implementing CFM measures dates back to 2010, when the six month holding period for transactions in the central bank bills was imposed, as well as a maximum of 30% capital to short-term offshore borrowings of the banks during that period[37]. This measure however was relaxed in 2013, following the Fed's taper tantrum, when the holding period for transactions in the central bank bills was shorten to one month. In addition, BI expanded the number of transactions which was originally excluded from the calculation of the offshore borrowing of the banks[38]. These measures have helped dampen the short-term and volatile capital flows during those periods. Furthermore, in 2014, BI introduced new regulations, which aimed to strengthen risk management of non-bank corporate external debt[39]. Banks were required to fulfill: (i) currency hedging ratio of a minimum 25% of their net external debts due within three and six months, (ii) liquidity ratio (including the current foreign assets in the hedging ratio) of a minimum 70% of their net external debts due within three months, and (iii) a minimum credit rating of no less than equivalent to BB-, as issued by a rating agency recognized by BI. Also, in order to strengthen the exchange rate stability and support economic development, BI introduced new regulation that requires Indonesian exporters and debtors to deposit their export proceeds and foreign exchange loans within Indonesia's monetary system through local foreign exchange bank. There is no obligation to keep these funds in a domestic bank and no restriction on subsequent transfers abroad. There is also no obligation to convert the foreign exchange to domestic currency. Since the end of September 2015, the regulation of minimum holding period for the central bank bills transactions has been adjusted from one month to one week in order to attract foreign capital inflows as part of the goal to strengthen foreign exchange supply and demand management.

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[36] See "Central Bank Policy Mix: Key Concepts and Indonesia's Experience" (2016)

[37] The measure of a maximum of 30% capital to the banks' short-term offshore borrowings was implemented for the first time in 2005 and has been evaluated for several times since then.

[38] The number of transactions excluded from the calculation of the offshore borrowing of the banks was originally applied since 2011, and adjusted in 2014, although with different objective, among others to support the strategic infrastructure projects (PSN) as well as financial market deepening.

[39] See "Indonesia: the macroprudential framework and the central bank's policy mix" (2017)

In 2020, recent global challenges following the COVID-19 pandemic have led to significant uncertainty in the global financial market and liquidity volatility perceived especially by the emerging economies, including Indonesia. During the early period of the pandemic in 2020, Indonesia experienced a significant decline in capital inflows, which led to Rupiah depreciation. In order to mitigate the pandemic's impact on economic growth and financial stability, BI has strengthened its policy mix through accommodative monetary policy by lowering the BI7DRR, liquidity injection, strengthening the monetary operations strategy, and directing the Rupiah exchange rate to be in line with its fundamental value through stabilization mechanisms called the "triple intervention strategy". This strategy has been implemented through an intervention on the spot market, Domestic Non-Deliverable Forward (DNDF), and purchases of Government Bond (SBN) from the secondary market. Moreover, accommodative macroprudential policy has also been put in place to maintain financial system stability, as well as to support the effectiveness of monetary policy transmission. BI also relaxed a number of macroprudential measures to support domestic economic recovery by (i) loosening the reserve requirement for banks that extend the loan to MSMEs, export-import activities, and priority sectors stipulated in the PEN (National Economic Recovery) program; (ii) easing the disincentive of the Macroprudential Intermediation Ratio (RIM); (iii) reducing Loans to Value (LTV); (iv) increasing the Macroprudential Liquidity Buffer Ratio (PLM).

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