

Seminário Internacional

Desafios e Oportunidades para a Integração Financeira e Monetária na Região

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Analysing the Integration of the Brazilian Financial Markets: Towards a Mercosur Vision

Dr. Claes Belfrage, Management School, University of Liverpool, British Project Consultant









Overview

- Research
- Development in Emerging Market Economies
- Emerging Market Economy Currency Internationalisation
- Lessons from European Integration
- The Vision: Mercosur's Virtuous Currency Internationalisation
- Report Policy Proposals

Disclaimer: These ideas are not those of the BCB, or the UKFCO









Research

- Currency internationalisation can bring benefits
- Risks with international currency internationalisation: vulnerability and procyclicality
- The damage can be negative effect on longterm growth prospects and credibility of strong and stable economy
- The stronger and more stable the economy is the greater the greater the ambition and benefits from Currency Internationalisation can be.
- Currency internationalisation (and financial integration) is *virtuous* when it is *complementary* to a broader growth strategy.
- The risks are particularly great for developing/emerging market economies: international monetary asymmetries
- Therefore, Emerging Market/Developing Economy Currency Internationalisation (and financial integration) has to be subordinated to a broader vulnerability-reducing development strategy.







Development in Emerging Market Economies

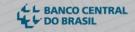
- China: Export-oriented industrialisation strategy; dependency on energy and commodities imports; global mass demand for exports. Financial integration strategy, including Currency Internationalisation (proactive), supports development strategy.
- South Africa: Economy centred on extractive industries, without clear development strategy. Dependent on commodity exports. Embraced financial integration, including Currency Internationalisation (full).
- Brazil: Growth strategy focusing on mix of extractivism, industrialisation and growth of domestic demand, but primarisation as growing dependency on Chinese demand for commodities. Cautious Currency Internationalisation (reactive).

Lessons:

- a) longterm development for EMEs is plausible when vulnerability is minimised
- b) Yet, inevitable (inter)dependence







Emerging Market Economy Currency Internationalisation

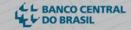
- South Africa's Full Currency Internationalisation: Not Complementary
- Brazil's Reactive Currency Internationalisation: Asupportive of development (ultimately not complementary).
- China's Proactive Currency Internationalisation: development- and trade-led CI (potentially complementary).

Lessons learnt:

- a) If unsupportive of a vulnerability-reducing development strategy, it becomes destabilising, which damages credibility of currency.
- b) Currency Internationalisation designed to support a development strategy which reduces vulnerability over time we call *virtuous*.
- Vulnerability could be reduced if development and virtuous currency internationalisation take place in cooperation with trusted others.







Lessons from European Integration

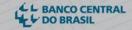
- Idea of shared development through industrial-functional and trade integration enabled by close cooperation and funding of infrastructure and joint market.
- European integration contributed to European golden years.
- "Full" regional currency internationalisation (EMU) followed uneven financial integration.
- Insufficient and improper macroeconomic convergence, banking regulation and political integration, despite some solidarity, were exposed in Eurozone crisis by financial market scrutiny.
- Regional currency internationalisation (incl. monetary integration) amplified these weaknesses.

Lessons:

- European facilitation of industrial-functional and trade integration was successful in supporting regional development.
- Monetary Union amongst sovereigns is almost certainly a recipe for disaster.
- Financial integration does not resolve underlying weaknesses in the economy, regional or national, political or social.







Vision: Mercosur's Virtuous Currency Internationalisation

- Mercosur should develop a strategy for regional currency internationalisation centred on the use of local currencies.
- This must be designed proactively so as to support a shared vulnerabilityreducing development strategy, which must be primary.
- The development strategy should focus on:
- a) industrial-functional and trade integration
- b) enabled by funding of infrastructure, research and innovation, redistributive development of skills and demand, market defragmentation and macroeconomic convergence.
- Mercosur currency internationalisation/monetary cooperation must be trade-led and incentivise commitment.
- Tailored financial integration can support integration process, but it cannot resolve underlying weaknesses in the economy, regional or national, political or social. It must include prudential measures.





Report Policy Proposals

- 1. Develop and extend regional payment, clearing, and settlement mechanisms
- 2. Commission a Study to Analyze the Risks and Opportunities of a more elaborate system of bilateral swap agreements
- 3. Enhance collaboration, macroeconomic and regulatory coordination, and harmonization between central banks and regulatory agencies
- 4. Commission a study of the costs and benefits of introducing regional currency derivatives to hedge regional exchange rate risk
- 5. Special credit lines mediated through specifically assigned dealer banks could enhance offshore settlement in local currency
- 6. Maintain countercyclical macro-prudential measures as part of the macroeconomic toolkit
- 7. Support the establishment of regional funding currency in the long term

Dr. Annina Kaltenbrunner will elaborate and add to this in her presentation.



