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CAPITAL CONTROLS AND THE WORLD FINANCIAL AUTHORITY
What can we learn from the Indian Experience?

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Abstract

This paper seeks to analyze the Indian experience with capital account liberalization and its regulatory structure of capital controls. In doing so, it examines some exchange rate policy dilemmas that arise to consider their macroeconomic implications. The main object of the essay, however, is to explore the interface between national regulation for cross-border capital movements and international norms for a proposed World Financial Authority that would act as a regulator in international financial markets. In this construct, capital controls are just another form of regulation of markets. It is argued that any framework for capital controls would need to be flexible. For example, quantitative controls or regulatory controls should be just as permissible as price-based controls. Even asymmetries in controls, between capital outflows and capital inflows, residents and non-residents, or individuals and corporates, which are discernible from the Indian experience, should be consistent with such a framework. Underlying objectives can differ between countries and change over time. Therefore, capital controls can range from prudential controls for crisis prevention and *ad hoc* controls for crisis management to safeguard controls for the balance of payments and developmental controls for autonomy in the formulation of economic policies. In conclusion, the paper suggests three fundamental principles for any framework to create a World Financial Authority. First, it should recognize that capital account liberalization is a means and not an end in itself. Second, it should provide for safeguards, not only to protect the balance of payments but also to manage the macroeconomic vulnerability associated with cross-border capital movements. Third, it should incorporate development as an objective, so that the international regime is conducive for the pursuit of national development objectives and does not reduce degrees of freedom for countries that are latecomers to development.