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## Systemic Liquidity Policies

### Proposed Contents

#### 1. Events Triggering Liquidity Problems

- *Shocks* in the financial environment.
  - Failure of one or more banking institutions, simultaneously, by way of contagion.
  - Denial of access to foreign financing to banks.
  - Volatility of international capital flows: changes in the overall liquidity of the economy, interest rates and exchange rate.
- *Shocks* in the commercial environment.
  - Slowdown in the level of economic activity or more expensive credit due to:
    - Sudden movements in international prices of strategic products being imported/exported.
    - Lower external demand for local products.
    - Sudden movements on the exchange rate.
  - Other kinds of shocks (political, natural disasters).
  - What indicators, whether macro-economic or sector-specific, help in evaluating the permanent or transient nature of an external shock so as to prevent the eventual translation of this shock into a real liquidity crisis?

#### 2. Mechanisms to Face Liquidity Crises

- Conditions that predetermine the efficiency and efficacy of policies to be used: short-term “trade-off” between policies to face financial crisis and the objective of price stability.
  - Public credibility in the economic policy: proven commitment by the central bank to fight inflation, by the economy ministries with the budget of revenues/expenditures, etc.
  - Transmission of the monetary policy: efficiency, depth, solvency and transparency of the financial system and, in particular, of the payments system.
  - Existing policies to regulate liquidity in the banking system.
  - Consistency, flexibility and opportunity, etc. of macroeconomic policies.
  - Price and wage flexibility.
  - Level of dependence on external savings.
  - Level of commercial integration.
  - Characteristics of the “safety net” mechanisms.
  - The role of the lender of last resort in normal times and in times of stress.
  - Mechanisms to protect deposits in normal times and in times of stress.
  - What is the perception of the overall citizen regarding the celerity, depth, discretionary or by-the-book nature of actions when applying these mechanisms at moments in which a potential crisis is emerging?
- Relationships between rigidity of regulation and the business cycle.
- Using international currency reserves, foreign loans and “financial armors”<sup>1</sup>
- Applying controls to international capital flows.
- Social communication strategies.

#### 3. Strengthening the Safety Net with the International Support

- IMF credit facilities/aid packages.
- Dollarization and/or monetary unions: where does the lender of last resort function rests?
- Other kinds of international support: the North America Financial Agreement.

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<sup>1</sup> To pay a fee/premium so that in case of contingencies funds may be obtained in conditions similar to those existing before the crisis situation.