

Abstract (summary):

Since the 1990s, the IMF has been persuading emerging market countries to avoid restrictions on their capital accounts to improve economic efficiency. As a result, some countries that pursued liberalization have faced huge currency crises due to premature liberalization. Some economists expect that imposing capital restrictions could create bad economic fundamentals: i.e., misallocating financial resources, which would eventually lead an economy to crisis. Some recent empirical analyses, however, have found that capital controls are positively associated with currency crises. Some other studies find no significant relationship.

These mixed empirical results could be the result of applying blunt capital restriction measurements, especially ones that do not allow for different degrees of controls. These studies also do not distinguish between controls on inflows and outflows although many economists expect these to have different effects. This dissertation creates measures of capital controls by increasing the disaggregation and intensity of capital control indices, and measuring separately the controls on capital inflows from capital restrictions on outflows. This makes use of the newly improved information about capital transactions from the IMF's AREAER started in 1996. The data of this study spans the period from 1995 to 2004, covering 26 emerging markets around the world.

The analyses of the association between currency crises and capital restrictions in this dissertation find that imposing controls on capital inflows (outflows) is more likely to reduce (increase) the vulnerability to currency crises, using Exchange Market Pressure Indices (EMPI) as proxies for currency crises. Due to a high correlation between the inflow and outflow capital control measures, the joint confidence ellipsoid (region) technique is used. This technique confirms that these capital controls have significantly different influences on currency crises. The analyses use various currency crises measures (dummy and continuous variables), various types of capital transactions restrictions, and compare these results against the capital control indices of well-known studies.