ISDA Safe, Efficient Markets

INSTITUTE OF INTERNATIONAL FINANCE

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Dear G20 Finance Ministers and Central Bank Governors:

The Institute of International Finance (IIF)[1] and its membership comprising broad representation of the global financial industry and the International Swaps and Derivatives Association, Inc. (ISDA[2]) applaud the significant efforts undertaken by the Federal Reserve Board (FRB) to provide temporary dollar liquidity to markets via the FX swap lines mechanism as well as the corresponding repo facility. These measures continue to have positive effects during the current COVID-19 crisis by helping local banking systems access USD in order to continue to finance USD positions.

As we approach the G20 meetings next week along with the IMF/World Bank Spring Meetings, our concern is that this dollar liquidity problem has expanded beyond developed markets (DMs) and the four emerging market countries (EMs) with whom the Federal Reserve currently has swap lines. Many other EMs potentially require increased access to USD liquidity since they face numerous challenges during the ongoing COVID-19 crisis. The knowledge of potential foreign exchange shortfalls might lead to a loss of trust in their local currencies, which could, lead to local currency depreciation. The USD liquidity need arises via three potential channels:

1. Deterioration of the current account
2. Reduced roll over of foreign exchange debt
3. Change in the 'dollarisation' level of the domestic financial system

The first channel relates to long-term imbalances, and there are existing mechanisms to address them at the international level. But the USD liquidity need driven by the second and third channels is driven by relative confidence in the ability of the local authorities to manage a sudden change in capital flows effectively. In the absence of coordinated efforts at the global level, national authorities might resort to restrictions, e.g., currency controls, moratoria on debt payments and similar measures. Such actions, in turn, may lead to a further loss of confidence by local and international market participants, and undermine hard fought progress to develop local capital markets.

[1] The Institute of International Finance is the global association of the financial industry, with more than 450 members from more than 70 countries. Its mission is to support the financial industry in the prudent management of risks; to develop sound industry practices; and to advocate for regulatory, financial and economic policies that are in the broad interests of its members and foster global financial stability and sustainable economic growth. IIF members include commercial and investment banks, asset managers, insurance companies, sovereign wealth funds, hedge funds, central banks and development banks.

[2] Since 1985, ISDA has worked to make the global derivatives markets safer and more efficient. Today, ISDA has more than 900 member institutions from 73 countries. These members comprise a broad range of derivatives market participants, including corporations, investment managers, government and supranational entities, insurance companies, energy and commodities firms, and international and regional banks. In addition to market participants, members also include key components of the derivatives market infrastructure, such as exchanges, intermediaries, clearing houses and repositories, as well as law firms, accounting firms and other service providers. Information about ISDA and its activities is available on the Association's website: www.isda.org. Follow us on Twitter @ISDA.

Calculating the impact on GDP would be highly speculative, but we assume it would be significant. An FX shortage could limit a country's policy space. Such a shortage constrains both fiscal and monetary policy responses to cushion the individual economies from the COVID-19 shock. Therefore, to enhance dollar liquidity for EMs and DMs, we would recommend that the G20 finance ministries and central banks work collaboratively with the IMF to take a series of actions:

- The Federal Reserve should expand its swap lines to EMs beyond the countries that participated in 2008, where appropriate, recognizing the FRB's concerns with taking on credit risk.
- The G20 should use its influence to increase substantially the "cap" of 50% of quota on the IMF's Rapid Financing Instrument, which works as a liquidity line for EM countries.
- The G20 should use its influence with the IMF to urge it to consider its existing facilities (or to create a new one) that would boost the reserves of EM and DM countries. This could allow those countries to take advantage of the FRB's new FIMA Repo Facility.
- To increase IMF resources, the G20 countries should accelerate approval of the IMF's proposal to double the New Arrangements to Borrow and, where appropriate, expand bilateral loans to the IMF.

IIF and ISDA would be glad to offer any assistance (including further analysis) to explore this issue further. We also stand ready to assist with the necessary transmission efforts.

Sincerely,

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