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P R O C E E D I N G S

MR. BEATTIE: Thank you all very much for coming. I'm Alan Beattie. I'm the international economy editor of the Financial Times here in D.C., so I have almost nothing to write about at the moment, as you can imagine. (Laughter.) We're here to discuss with very good timing central banking and how central banking might change.

Now, back when I used to be a central banker at the Bank of England back in the late 1990s central banking was actually dead easy. You had one instrument, which was a short term interest rate, you had one target, which was the inflation target, and anyone who suggested otherwise would be shot dead in the corridors at the behest of the governor. Meanwhile, banking supervision was hived off to a separate agency, the financial services authority, as it had been in most countries a long time before. And just to underline the fact that this was an entirely separate operation which was not going to be allowed to infect the setting of monetary policy, it was moved several miles across town.

I think it's safe to say that that model has now comprehensively broken down. Central banks largely failed to stop large credit bubbles blowing up during the 2000s, and they've now embarked on a range of measures that once would have been thought absolutely impossible, bringing interest rates to zero, setting quantitative easing targets, and of course as we saw from the Swiss National Bank last week, setting currency targets and not intervening in unlimited measures until they hit them. There is of course the added and related issue of how one central bank's policy won't spill over into other countries around the world.

So to discuss this, we have a range of eminent people, who are not just expert in the issues themselves but also have experience in actually running policy.

From your left, Andrés Velasco, who is the Finance Minister of Chile -- was -- who among other things created an innovative fund to save Chile's copper windfall. He is now as you can see now looking very relaxed in academia as a professor at Columbia University. Next to him is Raghu Rajan, again another relaxed former policymaker who was at the International Monetary Fund I think it's safe to say when it had a less exciting time than it has now and is now teaching finance at Chicago. Then we have Mulyani Indrawati, who if she's looking concerned, that's because she's still currently at this moment a policymaker at the World Bank, and before that she was Indonesia's Minister of Finance and enormously well regarded, and I have heard it said even treated as a rock star within the region. And immediately here is Eswar Prasad, formerly head of the International Monetary Fund's China division and now teaching trade and economics at Cornell University.

Now, the format for this discussion is we're going to hear from each of the panelists one by one. I will ask a few questions just to be provocative, and then we will open it up to questions from the audience. So to kick off, I think we're going to have Raghu.

MR. RAJAN: Thanks you very much. Let me tell you a little bit about how this group got together. First, I would like to thank the Sloan Foundation for agreeing to fund us and the Brookings Institution for hosting it. It started with a conversation amongst a group of us, primarily Barry Eichengreen and some of us, on whether we had anything to say as academics, former policymakers and so on the way the world was moving. One of the things we thought we could contribute to was to provide new ideas, but with policy relevance that were not so far afield, out in left field that nobody would take it seriously, and we thought we'd form a group. We went and asked a bunch of eminent people that we thought we would like in the group, and everybody said yes without exception. Then we started on the hard task of getting funding, but we found that the Sloan Foundation was very eager to help. Daniel Goroff was very instrumental in that happening. And then we needed a home, and Eswar said, "Why not Brookings," and that's where we got the home.

After that we had to start the hard task of actually doing something. That's when we realized that one of the difficulties in the eminent group that we had together is that we had a whole lot of generals and no foot soldiers. So the question became who's going to do the work, and fortunately everybody pitched in. The next question was how we reconcile different interests. There are people from all parts of the economic spectrum, many parts of the economic spectrum I should say, represented on the committee. And as Andrés kept saying during this process, a camel is a horse designed by committee, and we were in the process of essentially doing that.

But I think at the end of it we've got a report together which does attempt to, A, say something which hopefully adds to the dialogue, and B, that is not so far out there that it will have absolutely no influence. What we're trying to do really is raise some questions about the existing framework of monetary policy and propose what we think are legitimate concerns about it and ways that we might actually attempt a change. Clearly, we're hopeful that some of the proposals we make will catch on over time, and while a couple of them may be a little too optimistic at this point, it will actually have some effect.

So with that preamble, let me quickly walk into the meat of the report. Essentially, we start with a consensus that Alan to some extent laid out. The consensus emphasized, one, that there's really no tradeoff between inflation and unemployment, a long run tradeoff, I should say, or permanent trade off, that central banks are fine focusing on inflation, and in that process they do the best job they can in bringing down unemployment, that high and volatile inflation does suppress growth, so you want to target inflation, and that inflation disproportionately harms poorer sections of society, and again, that's another reason why it should be kept low.

This was sort of the consensus behind the focus on inflation targeting. And in addition to the argument that inflation was good for a country in its own right, that low inflation was good, there's also the sense that when a country focused on keeping inflation low, keeping its own house in order and allowing the exchange rate to adjust automatically in a sense allowed it to do the best contribution for the world. So you didn't have to have a separate eye on what was happening to the rest of the word as a result of your own policies. Everybody keeping their own house in order automatically resulted in a somewhat reasonable situation for the world.

I would argue that a lot of the concern about this form of inflation targeting has emerged because some of these things have been called into question. One, for example, is that when you focus only to inflation are you taking your eye off the ball on other aspects of the economy which would come back to hurt you. In this case, financial stability, sometimes focusing only on inflation takes yourself eye off the financial stability ball, and it may be useful to keep an eye on what's going on in terms of credit and asset prices also because it could come back to hurt you.

Second, sometimes focusing on what's happening only in your economy and doing the best thing by that economy could still have ramifications elsewhere in the world and not necessarily to the benefit of those economies. There are various ways spillovers could take place. One of course is through the effect of capital flows, which have become quite important nowadays, but there could be other channels through which these spillovers take place.

Increasingly, there are concerns that some forms of monetary intervention that are undertaken when normal channels of transmission in your economy aren't working could have heightened spillover effects, and by this I'm talking about actions like purchasing bonds, QE2. One of the reasons for undertaking it is because the normal credit channels of transmission are not working in your economy, but that also implies that any actions in expanding domestic liquidity will tend to spill over to a greater extent outside because your domestic channels of transmitting liquidity aren't working that well.

All those are reasons to rethink the whole issue of what should central banking try and achieve, what kinds of objectives, what kinds of instruments.

Let me spend two minutes on financial stability and then hand it over to Andrés. We argue in the report for making financial stability an explicit part of central bank mandates. Now, people say, "Well, another mandate? It's already implicit. Aren't they already paying attention to it?" I think there's some value to making it explicit, but it's not just putting it out there as an objective. We're also arguing that monetary policy is a legitimate instrument to try and achieve financial stability.

There are occasions when your strongest tool or maybe sometimes your only effective tool is the interest rate, and to use that to try and achieve financial stability should not be ruled out. You may sometimes undershoot your inflation target if in the process of doing that you create more sustainable growth by in a sense quelling the process by which credit flows into asset prices.

Now, people have argued against this view by -- let me just in a sense (inaudible) the argument. The argument is you're basically saying we should tackle asset prices, we should try and prick them, we should try and prick bubbles. But it's very hard to identify bubbles, and given that we can't identify bubbles we should probably not embark on this process of trying to lean against asset prices. What we've tried to say in this report is that's not the right way of framing the question.

The real question is whether asset prices are rising rapidly along with rapid credit expansion. That often proves to be a source of concern, and in that kind of environment the question you should be asking yourself as a regulator is: What if current easy financing conditions attenuate or reverse? Will we then get serious adverse effects on growth? And if the answer is yes, that creates an environment where you should be more open to leaning against credit expansion, against asset price growth. In other words, you're not asking are these asset prices fundamentally justified. Instead, you're asking is the credit expansion process sustainable, and if it does reverse what are the consequences.

I think this kind of question is important to ask, because otherwise monetary policy is allowing a very dangerous asymmetry. The asymmetry is when the asset price is booming, when credit is booming you do nothing because you don't want to stand against these recognized bubbles. But of course when the bubble is pricked and collapses you pull out all stops because of course growth is impacted. So it does create a put option, in a sense, for those who are boosting asset prices and it creates a dangerous problem for the world.

In the report we also present the use of macroprudential tools. One important aspect we emphasize is the need to try and enlarge responsibility for financial stability in the central bank. Again, this perhaps is adding to the central bank's burdens, but given that it is the entity that has the strongest tool at its command, which is monetary policy, it is important that financial stability burdens belong there.

And finally, when we talk about capital controls, we argue that the wrong question again from the perspective of capital controls is to ask whether these capital controls prevented the exchange rate from rising. That's often the metric by which capital controls are viewed as effective and non-effective.

We think the bigger role of capital controls on the rare occasion when they have to be used is more to ensure financial stability, that if capital is pouring in and fueling a rapid expansion in credit and also asset liability mismatches as well as currency mismatches, to try and put some sand in the wheels of capital flows so as to extend maturities, to change the currency composition, that's important for financial stability in its own right, and that's the way we should see the use of capital controls rather than whether it keeps down the exchange rate or not.

That's basically our first chapter on financial stability and why it should be made an explicit part of the central bank's mandate.

MR. BEATTIE: Thank you very much. Now let's hear from Andrés.

MR. VELASCO: Thank you. Before I get into the substance of the two chapters I am going to discuss for you, let me tell you first how much fun it was to participate in this project and how terribly risky it was in that what do academics and finance ministers know about monetary policy, which of course is the province of central bankers.

We're all aware that we're stepping into a terrain that is fraught with many complexities, but we do hope that -- at least I learned, we learned, and we do hope that you will learn as well that --

MR. BEATTIE: We have one former central banker.

MR. VELASCO: One former central banker, of course, who reminded us along the way a few times that he wished there were more there.

In any case, I want to discuss chapter three and four of the report. Chapter three has to do with spillovers. In order to criticize a framework you have to describe it, and of course describing it simply will make the criticism easier later on, so let me tell you how we characterize the state of play, the conventional wisdom.

The conventional wisdom is sometimes summarized by saying that over the last ten or twenty years countries were advised to follow an inflation targeting plus floating regime. You use monetary policy to target inflation, you worry about the things that matter for inflation like the output gap, and you let the exchange rate do whatever the exchange rate is going to do in a freely floating market.

In that way of looking at the world, which of course is a great deal more complex than this, but I don't think the description is entirely unfair, in that world the exchange rate is not a target for monetary policy. There's no feedback role from the exchange rate to, say, interest rates. And secondly, the policymaker does not have to worry about issues of international adjustment, the current account, the trade balance, and certainly not about things that fall outside the country, because presumably the exchange rate is moving around to take care of those things.

So if the current account deficit is too large or if the trade balance isn't a large deficit, the exchange rate will move around and fix that. The only circumstance in which the policymaker should worry about the external central variables of the exchange rate is in so far as they may affect either inflation directly or indirectly via the output gap. Even for a small open economy, the prescription is to focus on domestic variables and the foreign variables to a large extent will take care of themselves.

In this framework, the possibility of international spillovers of course is recognized. If you go back to the 1980s there's a very large literature on issues of international policy coordination, et cetera, et cetera. However, we think it is fair to say that they do not take center stage, that they're really marginal as opposed to central in the way you conceive of the world and in the way you carry out monetary policy.

The other part of this conventional wisdom, although this is seldom made very explicit, is really a hope that countries gradually would adopt this worldwide. This began of course in Europe and quickly moved across the English-speaking world to places like Canada, Australia and New Zealand and moved very quickly to most if not all Latin American countries and to some of the smaller emerging Asian economies.

However, it did not become as widely spread around the world as some of the IT advocates had hoped. We have a graph in the paper showing that in fact the share of world GDP and the share of world exports covered by countries which are not under this regime is in fact growing over time. Part of it of course has to do with the fact that China is a much larger country as a share of the world economy and China does not have a floating exchange.

Now, what are the implications of this? One implication is that in the absence of convergence toward floating worldwide, the exchange rate has not served as an effective tool for international adjustment. One outgrowth of that is that we've had a number of years with very large and reasonably persistent current account imbalances, the global imbalances that people talked about so much.

Those were very large before the crisis, and they came down of course as demand in the deficit countries like the U.S. or the U.K. collapsed during the crisis, but they've come back up, and we'll see what the IMF says next week. But in the recent IMF economic outlooks there is a forecast of imbalances growing slowly again as you look into the future.

So first, deviation from the framework, we don't have convergence in IT plus floating regimes, and therefore the exchange rate does not play the role that it was supposed to play. This gives rise to all kinds of international issues because it gives rise to collective action issues, and if you do fix you don't only affect your citizens, you're affecting other people. For instance, countries in Asia compete with China in third markets for exports and worry about whatever is going to happen with the real exchange rate of China. And of course it has given rise to something that is less academic sounding but which has made the headlines, the so-called currency wars in the phrase coined by Brazil's Minister of Finance.

The second deviation from the core framework has to do not with the existence of spillovers but with the size of spillovers. We've known all along that spillovers would happen. We've known all along that financial flows typically dwarf trade flows. However, the size of potential spillovers seems to be growing over time, and we make three arguments in the report that try to underscore this case for a larger and perhaps more cumbersome and more dangerous role for spillovers.

The first one is the sheer size of financial flows and the existence of a very large pool of very intrasensitive funds out there ready to go to any country which has higher interest rates. Where does this footloose capital come from? Simply from the persistence of global imbalances. Countries that run current account surpluses accumulate assets, those assets sit in central banks and sovereign wealth funds and elsewhere, and they're looking for yield. So one can make the case that today financial flows play a larger role than they did when the framework was crafted fifteen or twenty years ago.

Secondly, we argue that commodity prices also play a role in transmitting and furthering these spillovers. Loose monetary policy in the major systemically important countries, among them the U.S., arguably has a role in beefing up commodity prices, and of course there's a big and heated debate on this. But a not too radical view would be to say that in a world of scarce assets, this is a view associated with Ricardo Caballero of MIT, this liquidity is looking for things in which to invest, assets into which to invest, and pieces of paper linked to the performance of commodity prices are one such asset. There's big demand for these assets, and this arguably keeps commodity prices up. But of course if you're a commodity producer and suddenly the price of your exports has gone up, then your more creditworthy capital is going to flow into your country and the spillover issue is going to be magnified, so there's an interaction between commodity prices and financial flows.

The third channel which arguably has increased the role of spillovers has to do with crisis times. We argue that in crisis times spillovers are larger than in normal times. When countries are in financial crisis or close to it and they engage in non-conventional monetary policies, there's a risk that a larger share of that additional liquidity will go overseas. Why? For a number of reasons.

One is that credit demand is weak locally, and a second reason is that local banks are especially reluctant to lend at times of financial distress, and therefore for every dollar you pump into the system a larger share of that dollar may go out into the Brazils or Indonesias or Colombias of the world than would be the case under more normal circumstances. So we do think that spillovers are an issue, we do think that spillovers are larger than was once thought, and we do think that spillovers therefore provide a case for rethinking this framework and also for tackling head on the collective action problems that arise from the existence of spillovers. In the concluding sections which I will not talk about there are some suggestions on how to deal with that.

That's chapter three. Let me just say a couple of things about chapter four. Chapter four simply aims to recognize that there are some new and important challenges to monetary policy which, precisely because they're so new, again may not have been fully taken into account when we thought about inflation targeting plus floating a decade or two ago.

The first challenge is most present in rich countries, and it is the challenge of large public debt. Of course, having weak fiscal policy and large public debts has always been an issue for monetary policy. Being from Latin America, I'm perfectly aware that the link between monitoring fiscal policy has a long and distinguished history. We invented it. Or not quite, but we perfected it, and therefore in some sense this is not an issue. What is new is, again, the size of some of these debts and the fact that they're prevalent today not in emerging nations but in developed countries.

The report argues that perhaps some of those tricks that were developed so cleverly in places like Latin America may be finding their way toward developed countries. It is not so hard to envision, and some of it is happening already, how you might provide incentives for local banks to hold government bonds or how you might provide incentives for pension funds over which the government has some say to hold government bonds. This of course was done in history, not only in Latin America, but in the U.S. in the 1940s for instance during World War Two. It has been used in many other quarters of the world. The question is to what extent will it be coming into fashion.

And of course the other link between monetary and fiscal policy nowadays which is most evident in Europe, when you have a large public debt some of that public debt is short maturity and yields jump, and there is a risk of financial instability and there's a large incentive for central banks to intervene and buy pieces of paper issued by others. In the case of Europe we've seen many -- how can I phrase this politely? -- turn or shifts of emphasis on what the ECB was willing or not to do, and today we find the ECB buying large quantities of Spanish paper, Italian paper, the kinds of things that the ECB said would not be done just few months ago. So we argue that this is a new and difficult issue with which central banking has to wrestle.

The other issue with which central banking has to wrestle is really lies emerging markets, and I've mentioned it already so I'll just kind of enunciate it, has to do with real exchange rate appreciation. Within our group there were voices, Danny Rodericks probably most eloquently, that argue that growth in emerging markets is very tightly linked to competitive exchange rates, and therefore allowing the real exchange rate to go anywhere is not good policy, and therefore this ought to be within the kinds of things that central banks worry about. That was not a view that commanded unanimity but which did carry a fair bit of weight, I think, within the discussions.

Again, to the extent that this is a political issue, there are political pressures brought to bear on central banks. And just as in the case of public debt, one has to ask the question, "Well, are there threats to central bank independence coming from the issue of Dutch disease in de-industrialization and real exchange rate appreciation." These are two very difficult issues, we don't claim to have a recipe for solving them, but we do say three things. I will mention them briefly and I will stop.

The first thing we say is that central banks would be well advised to admit that these are issues. As the report phrases it -- and I didn't write this paragraph, but I think it's a very good paragraph -- central banks should not play the game of "Who, me?" in this regard. These are real issues, and to the extent that central banks are perceived to be skirting the issues, to the extent that central banks are perceived to be part of the problem and not part of the solution, the political pressures brought to bear on central banks may become even larger, and therefore the threats to the independence of the central banks may become even larger.

The second thing we say is that central banks should be crystal clear that they can play a role in tackling these issues but they cannot play the role alone. Surely if the problem is too much public debt, fiscal policy is the first lever. If the problem is financial instability, regulation is the first lever. If the problem is real exchange rate appreciation, well, a tighter fiscal policy is also important. So monetary policy can play a role, but only alongside regulation, fiscal policy and a number of other policies.

And the third thing we say is that if central banks are going to veer into this mined and tricky terrain they should be even more careful than usual in communicating, communicating, communicating. Monetizing public debt and providing liquidity assistance to governments can be observationally equivalent, and one does not know which one a central bank is doing unless a central bank tells us what the central bank is doing. Even then we may not know, but at least the central bank should try. So the third message is communications, communications, communications are even more important in this terrain. These are two additional challenges to monetary policy which in our view provide yet one more argument for broadening this IT framework which has served the world well, but needs some rethinking at this point. Let me end there.

MR. BEATTIE: Thank you very much.

MR. PRASAD: So my task is to selectively summarize a few of the conclusions we arrived at after the analysis that Raghu and Andrés laid out so clearly. But let me preface my remarks by making two observations. One is that with this committee of very distinguished people, all of whom who had very strong views as was mentioned, there were differences of view, so we had two possible strategies. One was a "letting a thousand flowers" or maybe a "letting sixteen flowers bloom" strategy, which would have made the report very diffuse, or basically try to find language that everybody could agree on, which may have made the report much less interesting.

So what we've done in the report is basically lay bare the areas in which there were differences, but the process that Andrés and Raghu talked about was actually very useful in terms of all of us getting together and sort of understanding these different perspectives. It turns out in the end we didn't have that much dissension in the group in substance, and when it came to the conclusions, as you've seen, everybody has signed off on these conclusions. The second issue is that through these recommendations we hope to make it safer for people who want to walk the corridors of central banks without getting shot just because they think about multiple mandates or multiple targets.

There are different aspects of the recommendations that we tried to bring together. And as Raghu pointed out, it's not like we live in a world where central banks are purely targeting inflation. Even those that do claim to target inflation, they do look at a variety of indicators and they do have multiple objectives. But the sense we got from the discussions and talking to central bankers in the field is that there isn't a good framework to guide many of these issues, and that essentially is what the report aims to do. Not all of it is revolutionary, but it does try to bring it together all in one place, to put it all together in a framework that I think will help guide future discussions.

The first set of recommendations is really about how financial stability ties in with the narrower objectives of price stability or the sort of dual mandate that the U.S. Federal Reserve has. As Raghu pointed out, our view is that it's a very artificial separation, especially given what we've learned from the crisis, that thinking about macroeconomic stability and financial stability separately doesn't work. But operationally we still need something to hang on to, and the issue here again is not to think about identifying or pricking asset price bubbles, because in the best of circumstances these are difficult to identify, but the issue, again, is to try to put together more clearly frameworks in which credit expansion can be looked at along with asset price changes in order to deal with potential problems that could create not just financial but also macroeconomic instability.

One big issue, then, is where exactly the mandate for financial regulation should lie. As Raghu pointed out, we feel that it should be an essential part of central banking, but the institutional mechanisms in many countries are set up such that there is a separation. And again, one thing the crisis taught us is that whether it's the financial services authority in the U.K. or a different sort of model like in the U.S., where the Fed regulates the banks as well as runs monetary policy, it's not obvious what the right answer is. But one thing that is absolutely clear is that monetary policy does have a very important role to play in financial stability, and regulatory policies do have a very important role to play in macroeconomic stability, so finding mechanisms to have these two sets of policies mesh together is really what we intend to drive at.

Getting the right mix between prudential and monetary policies is really the focus, although we lay out in different scenarios how exactly this could be achieved. But with these multiple mandates, especially the mandates as to the central bank, as

Andrés pointed out, there is the concern that a proliferation of mandates basically makes a central bank more subject to political capture, and we think in fact that with broader mandates independence of the central bank or operational independence becomes much more important.

But central banks again don't operate in a vacuum, and central bank independence is not a (inaudible) per se. Central banks do operate in a political context, but what is crucial there is accountability. So once central banks do have a broader set of mandates the question is how one comes up with a mechanism whereby they do have the operational independence and yet are accountable to the political discourse. Again, this is where we think this report might have a useful role to play in terms of thinking about why a central bank focusing just on an inflation target may actually not be doing its broader job of maintaining macroeconomic and financial stability.

The issue of better communications, then, becomes much more important, trying to think about how these multiple mandates hang together and how the use of these multiple instruments works. In times when you have asset bubbles and expansion of credit, there might be a case for a tightening of monetary policy even if it means a shock in deviation from a clearly specified inflation target. It's in that context that we think that this multiple mandate approach may actually give the central bank a lot more leeway in terms of achieving these big objectives.

The other crucial issue which Andrés talked about is spillovers. We live in a world now where it is impossible for large central banks, central banks of large economies, not to have effects on other economies. But ultimately a central bank is responsibility for policies and outcomes within its own country. How do we reconcile this difference?

The problem right now is that there isn't a forum or even a framework for asking certain types of questions. For instance, one can ask the question, Is U.S. policy monetary policy or the setting of U.S. monetary policy good for the U.S. economy." Or one can ask a different question: "Is the setting of U.S. monetary policy creating complications for emerging markets, the sort of currency wars that were referred to earlier." But we don't have a good framework for asking is U.S. policy in a general equilibrium sense really good for the world at large, because if ultimately the U.S. does not do well, and it's a very large economy, that has significant ramifications on the rest of the world. But these questions tend to be taken apart rather than pieced together.

So what sort of institutional mechanism could do this? Again, the concept is much more important here than the precise formulation of how we think it should be done. But one way we think it could be done is through setting up an international monetary policy committee, perhaps the central bankers of the ten or twelve largest economies in the word, the six large reserve currency countries, as well as maybe five or six of the central banks. Perhaps this is one way that having this group basically think about how the mutual consistency of their policies could be helpful.

These central bankers do meet in a much more formal setting and in a much larger group, but we think there might be value to having the key central bankers in the world basically try to explain to the world at large, including to their own political leaders, how there might be inconsistencies in their policy settings and how both domestic policies and policies of other countries could potentially be reconciled.

This is going to become important even if we move to this idealized world. As Andrés pointed out, we're nowhere close to this, so to speak, idealized world where every country has a price stability objective for its central bank and its flexible exchange rates. But even if we do get to that idealized world, these questions are going to become very important. Because, again, if you have one country that needs loose monetary policy, especially if it is a large country, that has significant effects on other countries that may have a need for a very different policy setting. So ultimately, I think even if it's not really coordination, having a forum to bring out these tensions I think is going to be important rather than just this (inaudible) in these currency wars.

The second set of recommendations is much more tightly focused on financial regulation, and Raghu has laid out many of these issues. There basically we take the consensus view that many of these macroprudential measures that have been discussed in the literature, including specific measures like using loan-to-value ratios and debt service to income ratios with appropriate cyclical adjustments might be useful.

But one thing we do emphasize in the report is that all of these do sound very good. Contingent capital buffers do sound very good, countercyclical capital requirements sound very good, but the effectiveness of these tools still remains to be tested, and this becomes especially difficult when thinking about coordinating these policies across countries. This ultimately is going to be a crucial issue, thinking about how one coordinates these policies, because given the nature of financial integration across the world, thinking about these policies in isolation doesn't work very well. Here again there is a tension. The tension is that trying to get to a standard that all countries can agree to might mean a very watered down standard. And there is a lot of stickiness in the initial conditions given the very powerful forces that are arrayed against certain types of reforms.

So our recommendation is that countries should at least agree upon a broad framework, a set of policies that they all put into place, and then based on country-specific conditions these can be adjusted up or down. Ultimately we think this coordination is going to be a crucial issue.

The third set of recommendations directly touches upon the issue of spillovers. This is where, as you can garner from the earlier discussion, there was the most disagreement among people from different schools of thought, people who had been on the front lines in different segments. The general view of the committee was that we do live in a world where taking instruments like capital controls completely off the table is the level of purity or intellectual or ideological purity that is simply not warranted by the practical difficulties of the world we live in.

Nevertheless, a lot of people on the committee were very concerned that tools like capital controls could be effective if used in a prudential sense if applied uniformly across domestic and foreign investors, as the IMF for instance has been arguing. But these are going to become much less effective over time. Capital accounts are becoming more open in de facto terms. Financial institutions are having much broader operations. So the sense that capital controls really provide an important line of defense I think is becoming increasingly untenable. We think this might have a role at the margin in terms of smoothing out volatility, but there are really no substitutes for the more fundamental reforms that are needed.

But also the sort of forum that we think about, the international monetary policy committee, may be a way of thinking about what the implications are for individual countries' policy settings as well as their mutual consistency if a number of countries start undertaking these policies at the same time. Again, this is where the sort of the committee approach we recommended earlier we think might be very useful in sort of putting these tensions on the table in a more direct way rather than just degenerating into public conflicts. And as Andrés pointed out, financial repression is again a major concern that we caution about. As a team member, Carmen Reinhart, has pointed out, a lot of what is going on in the form of regulatory policies does have an element of financial repression to it, and this is something that clearly needs to be guarded against.

So ultimately, the report does have a number of very specific recommendations which I will not go into in much detail. But the question is whether, again, we have set out a lot of new things on the table, and what I would emphasize again is that rather than the particulars of each recommendation, the concepts that we're putting in place are I think far more important because we think these serve as a basis for discussion. One might in a cynical way argue that this is just theory catching up to practice, because central banking in practice is a lot more flexible and pragmatic. But again, there has been a guiding framework, which is that of inflation targeting or a single price stability motive, a price stability objective with flexible exchange rates, and we think it's important for theory to sort of provide much more coherent guidance to the practical approach that the central bankers are taking these days.

MR. BEATTIE: Thank you very much. And now to respond to all of those comments, Ms. Indrawati.

MS. INDRAWATI: Thank you very inviting me. This is really interesting, especially for me, coming from Indonesia, who actually tried to adopt in the past the technocratic framework. There are a couple of things that I will try to comment on in this case. First is the central bank focusing on one single objective for global price stability. Many of the small only economies have been shifting their thinking, and they're the ones who adopted this thinking that you should focus on price stability, which is going to increase more credibility about your monetary policy. That is also the result of, as you call it, the Asian financial crisis in '97 and '98, which is that they needed to specialize the central bank into one single focus. That is one thing, if we can call it in the past fifteen years or twelve years, to indicate the stability of the inflation, that the low inflation environment is there. There are many developing countries and emerging countries adopting that framework and again the credibility of the stability and low inflation environment, although maybe you could argue also that this is a result or achievement because of the role of China, which provides very low and cheap manufacturing goods all over the world.

That is one achievement, and we certainly support that having clarity about goals and instruments with this one-on-one relationship is going to create a clearer result, but also at the same time also a certain credibility. But at the same time, the problem of the financial crisis is not purely because of the value of the aggregate level of the credit expansion of the asset bubble, but also because value of the prudential regulation enforcement, and many of them are also related to governance problems.

Now we try to avoid this concept of using the monetary policy in order to also achieve the financial stability. We raise the issue about whether this accountability, which was mentioned earlier, is going to be easily detected or in this case for the central bank, especially because at the same time the central bank has their own self-interest. Definitely a central bank is not coming with all credibility and respect in the sense that they are seen as the most successful in managing the economy and contributing to the stability. There are quite a lot of reasons also in questioning about the internal checks and balances as well as governance with the central bank, that they are going to avoid what you call a conflict of interest of having too big authority within themselves.

This is one thing that also needs to be questioned in terms of adding up in this fashion with most of the small open economies trying to focus on the price stability, and now they are adopting, and in this case accommodating the new fashion of price stability. For example, Australia has been very successful in having a separation of the functions. This is not because this is supposed to be in one institution like the central bank. It can be in two different institutions like the central bank and a financial supervisory agency.

Sometimes it is a problem of personality in which they can communicate well, in this cases it could be the institutional arrangement. But I think I can understand the spirit or the objective of this paper or of this proposition. It is that you need to have these two always working together. Pragmatically it's definitely there. You cannot separate, and you don't have the laxity to have one instrument and one objective anymore when you are dealing with the complex economic environment and the policies which interact with each other. I personally can understand the proposal, but it will be very difficult to translate it within the institutional setting. That is going to be my second comment.

When you put it into the institutional setting, the central bank -- I think we have to look at what is the value as well as the success of this kind of arrangement, and that will test the issue of the institutional arrangement governance and the effectiveness of all of this if you talk about at the national level first. And that's why I think separation. I will use the Indonesian experience. This is a real experience, and changing the institutional setting mandate is not easy. Politically it will take a long time.

We had a financial crisis in '97 and '98 for Indonesia, and at that time the conclusion, including within the IMF package, was that you have to have the central bank which is focusing on inflation targeting and focusing on monetary policy, and the regulatory and all the supervisory is going to be separated. Along the way, until even now, if you look at Indonesia, this function of supervisory regulation is still within the central bank, because even over ten years the central bank can still lobby the politicians to say that you should not separate us.

And even with that, I must say that it is not always successful in actually relying on them and really watching for us. And excuse me, because I was not the central bank, I was a finance minister who had to pay the bill for whatever the central bank was doing, but the question regarding the institutional setting within one central bank is not about whether you trust them. They can be used pragmatically and effectively in managing both financial stability and the macroeconomic stability that is a low inflation environment, but you are questioning regarding whether they have the right that they can assume that huge responsibility and authority with a very minimum accountability or checks and balances.

That is especially true in many countries. And whether this is related to the central bank or you are dealing with a very big financial institutions, they have a huge potential ability to influence the political forces surrounding them, that they will (inaudible) in order to favor that position rather than really that you are having a noble idea, that they're really thinking about a very good noble objective of maintaining the economy of the country.

So they are just the same bunch of people and they have a lot of power, and the power, if it goes unchecked, it is going to be corrupt in a way. This is one thing which is going to be that in the political reality you have to look at it in terms of this dilemma about providing all these functions and all this authority vis-a-vis the checks and balances and accountability. That is my comment.

The second one is actually in terms of putting this within the context of the effectiveness. I guess in this case if we try to look at other countries which are quite successful, although they have two separate institutions, actually it's been driven by a good personality, the central bank governor as well as the FSA or whatever, as well as there is an institutional tradition which makes sure that the flow of information between the macroeconomic stability and financial stability is going to always be shared. And then at the same time, there is an institutional mechanism in which they are going to respond in a more coordinated way in order for them to identify what is the vulnerability, the asset price, or in this case something which will (inaudible) whether this is macroeconomy or financial stability. It is really driven by this communication.

My third comment is on the proposal of setting up the international monetary policy. I think I question this kind of proposal, given the setting which we are having. I was actually involved in the G-20 leaders' forum in the middle of the 2008 crisis. The question is are you asking about more fora or is this a mechanism that will ensure that you are going to have the policy coordination. If it is only a forum, you have the IMFC, you have the IMF already in this case, or even in this case adding up to that you have the G-20, you have the G-7 and the G-8, in which you are actually dealing with so many fora it is not like a forum.

I think in this case the question is what makes them fail to become the real effective forum or body or institution that will make them able to have a standing as well as the ability politically to act and to make decisions which will gain a much bigger benefit for global economic stability, prosperity and so on vis-a-vis the cost which they have to face immediately. Each of the policy choices definitely has an immediate cost, and that cost is usually the one which is unbearable. Unfortunately, I think in this case my observation is that this is not about the forum. This is about the mismatch between the fact that the global economy has become globalized, you talk about capital which is borderless, but at the same time each of the regulators and policymakers is still governed by their own sovereign status.

So we are actually faced with a critical question globally now, that we may be so successful in globalizing so many things, but the ability of the sovereign mechanism to actually deal with these consequences is not there, so you are going to deal with so many mismatches of these two institutional settings. You talk about how you try very hard for every country for example making the straight agreement, you try to liberalize, you adopt the free capital flow, but it's always like left behind with the consequence of all this globalized thing, whether you're talking about goods, capital, and even now people, and information is definitely there. I think this is more on this mismatch and the question of whether this kind of forum is going to match with this real problem that we are facing at the global level. That's my comment.

MR. BEATTIE: Thank you so much. I just wondered before I start asking questions and opening up for questions, if any of the panelists would like to respond to any of the points that the respondent brought has brought up.

SPEAKER: Just quickly on this last point, I think the point is very well taken: What do we gain by one more committee.

MR. BEATTIE: I'd like to second that, by the way, as a journalist who covers lots of committees.

SPEAKER: And having been through many of these committees, I think members on this panel are pretty aware of how few times many of these committees are. I think there are a couple of things we wanted to emphasize. The existing committees talk about a lot of other things also, and typically the discussion rarely gets focused on monetary policy. I think we're exactly on the point where you ended up, which is that with the globalized world there is a global monetary policy stance. Nobody has responsibility for that. Nobody is talking about how these things add up. And we have no illusion that at this point asking the U.S. Federal Reserve to take into account what happens as a consequence of its policies more than at second or third pass, it's not going to happen. Similarly, China and its exchange rate policy, they're not going to worry too much about what its external effects are, and that's the reality.

But what we're hopeful about is getting -- I would defer a little bit from Eswar in saying the number has to be even smaller then ten -- whenever you get more than five, they don't really have a discussion -- but getting a small number, which then has to come out and say, "This is what we see the global stance at."

The first pass is actually getting them to come out with a common statement recognizing where the differences are and where in some sense they see the challenges. It doesn't mean any one of them does anything about it, but at least they recognize explicitly the challenges.

Right now I think the view in many of these international committees is broadly that each country is allowed to have its own monetary policy and we don't worry about the spillover effects that much, other than every once in a while we complain about currency woes and so on. But having them come together and regularly put out a statement can then form the basis over time to recognize that yes, this is incompatible, and yes, we should be acknowledging this much more in our domestic policy stance.

That's when you start getting more of a sense that maybe it might be legitimate to have a spillover question being asked within each country, and that's when monetary policy could adjust over time. It's not going to happen tomorrow, it's not going to happen next year, but maybe ten years from now when you're forced to do this and you recognize the incompatibilities we might eventually get to a place where you might have some bite.

MR. BEATTIE: Before I open it up, let me just ask one question of my own. Picking up on a point that both Andrés and Eswar made, which is we talked about the paradigm of inflation targeting and interest rates and the floating exchange rate, and of course you both pointed out that large parts of the world didn't actually have that, and many people would blame that for a large part on the financial crisis in the sense that the cheap money that was being shoved at the American consumer by China, for example, was one of the things that puffed up the credit bubble, and it's obviously impossible to go back and re-run the world a different way, but had that paradigm been universal so that it had been adopted by China, how much of this do you think we'd be talking about now? How much of that problem would this have solved?

MR. VELASCO: My instinct is to say that it takes two to tango. If you've ever been in a finance ministry or any kind of policymaking position, you spend a fair bit of time answering the phone and trying to tell investment bankers that no, you did not want that extra billion that they were offering.

If emerging markets were able to turn the investment bankers away, one would like to think that emerged markets would have been able to do the same thing. So yes, when you have a lot of liquidity floating around, that is a problem, but it is not a coincidence that the liquidity found itself into some corners of the world, the American real estate market or the Irish real estate market or the British or Spanish real estate markets with all the consequences we know, but it didn't make its way into other corners of the world.

There are countries in which there was a bubble and the bubble burst, and there were a bunch of countries where that did not happen. The countries where that did not happen coincidentally were mostly countries where it had happened a decade earlier. I suppose there's a theory in economics that says everybody will have a financial crisis and will have it soon and therefore learn the lessons. In Latin America we had our financial crisis in 1981, '82 and '83, and we learned full well that bankers should be kept on a very short lease. That was heralded obviously back then and is conventional wisdom right now.

SPEAKER: I think I'll divide your question into two parts. Number one: Is a single-minded focus on price stability one of the determining factors of the crisis now? Again, any central banker will tell you that even if they have an inflation target, a pure price stability objective, they do look at everything insofar as it affects inflation. So if asset prices are rising very fast, it affects consumption and therefore affects future inflation. But we feel that there is a pretty strong basis for making a stronger statement that before the effects of the inflation can be felt, rising credit expansion and asset price increases can boom and bust, creating fairly significant and large boom/bust cycles in the economy, so we think the inflation targeting approach needs to be made even more flexible than it already may have.

The second issue comes to this question of if everybody was doing, so to speak, the right thing, if everybody had been doing the right thing, having a price stability mandate for the central banks and running inflation targeting regimes with flexible exchange rates, I think this is where our report aims to be forward-looking. We are far from this ideal, but once we get there we're going to have to confront these issues about spillovers even more forcefully, and we're trying to think ahead about what sort of mechanisms are going be needed to deal with that issue. Once upon a time, Raghu was my boss so if had said (inaudible) to I had to say, "Yes, sir." Now we're all academics so we can all disagree.

Again, the number of central banks is not the core issue here, but the key issue here again is whether we have some forum to focus on this issue. Dr. Indrawati has correctly pointed out that an additional committee and another trip for central bankers is far from the desired thing, but I think having a forum where the focus is specifically on the spillover effects of domestic monetary policies is something that is going to become increasingly necessary for the world.

MR. BEATTIE: Thank you so much. If I could now open it up.

SPEAKER: I'm (inaudible) Singh. I've been working with the World Bank for a very long time. Right now I deal with the independent evaluation office of the IMF. The views I'm expressing certainly are mine. First, an observation. I think it's a good report, very meaningful, a good tie-in, but I'm surprised to see hardly any central banker in this group of sixteen here. I would have expected in a report at this point of time when we are just getting into another crisis or coming out of one, central bankers who would have had the experience of working through this and then contributing to this report would have been very, very interesting. Why do I specifically mention this? Because one of the key findings of your report saying financial stability should be a mandate probably could already be included in some of the central banks like the reserve bank in India.

Now a question. I was expecting from Velasco of course something to say on international reserves. And of course when he spoke about the commodity exporters, there by itself you get two sets of countries, and therefore I was expecting to hear something on international reserves. Thank you.

MR. BEATTIE: Would anyone like to respond to that?

MR. VELASCO: I guess precisely because we keep having crises, central bankers are too busy running the world. They don't have time to be writing reports, I suppose. But no, you're absolutely right. At the outset I said that academics or finance ministers or former finance ministers to step onto this difficult terrain is a tricky business. But let me add that precisely because central bankers talk to central bankers a lot, it is not an entirely futile exercise to have non-central bankers try to catch the attention of central bankers. Whether we will catch their attention and they will smile or whether they will bark, I'm not quite sure, but we are hoping that we will catch their attention.

International reserves. The issue is not explicit in the report, but it is certainly lurking in the background. Eswar mends it in passing. And it is relevant in connection with the issue of exchange rate appreciation in emerging markets. If you believe the purest simplest version of the IT plus floating approach, then there is no need to have reserves because you will never intervene. But in reality, most countries that float also have reserves, which tells you right away that the purest and simplest version of the framework is not being used practically anywhere. If you look at the last ten years, practically every floater has intervened at some point. Certainly Switzerland has recently caught our attention, but in Latin America we floater intervene, in Asia they floater intervene. New Zealand may be the only one that hasn't, I'm not entirely sure, but the bulk of countries do, and therefore you need reserves.

How large a set of reserves you need is going to depend exactly on what you're going to do with them. In my view, and this is not something that is in the report, is that your reserves are really there not only to allow you to intervene in the currency markets, they're there to allow you to serve as lender of last resort to the banking system.

Now, once you begin discussing these issues you're immediately I think into a discussion which takes you beyond the pure simple regime. All of these things are not within the regime. In practice they do happen. One contribution of the report is to say, "Look, we're doing things that we're not talking about, they're confusing, markets do not quite know what central banks are doing." If we have a language, a forum and an acknowledgment that these are reasonable things to worry about, then clarity and transparency may be well served and the effectiveness of policy may be well served.

SPEAKER: Thank you. My question is you are talking about the coordination for the central banks, but usually central banks tend to be a second mover, so first, I look at the fiscal policy, at the plans, and then the setup of the policy. If you look at this (inaudible) regime thing, usually it's the governments that decide about effects of the regimes and the central banks only execute this, so maybe we shouldn't talk here about the coordination of the central banks but rather coordination between the governments. Thank you.

MR. BEATTIE: Anyone like to pick up on that?

SPEAKER: (Inaudible) with the World Bank, formerly with the IMF. I think that having a multiple objective for central banks is long overdue, and I think it's beginning to be very well recognized, but why stop at looking at financial stability exchange rate misalignments and monetary spillovers? What about unemployment? Isn't that a big concern across the world? Shouldn't that be reintroduced as an objective as well?

And the question also is since coordinating macro-stability, actually there is an international organization in charge of that, it's the Fund, the IMF, and it has not only central bankers but also ministries of finance. I don't know why you picked the Bank for International Settlements over the IMF for this, for your committee.

SPEAKER: What we said in the report was that we would like this committee to be set up primarily tasked with talking about the global monetary policy stance, including issues of liquidity et cetera. Where it is located, who it presents a report to, how frequent that report is, all that we have left delightfully vague, which is why we can have a discussion here about how many members there are of that group. I think what we want to emphasize, and this goes back to the earlier question, is that it is important to recognize the incompatibilities and put that front and center out there. And then how we adjust to that, whether we alter domestic mandates over time, those are things that need to be addressed, but first let's recognize the incompatibilities. Let's start one step at a time.

So whether it's the government that has to do it or somebody else, let's first say monetary policy is incompatible, whether it's because regimes are incompatible. Whether it's because regimes are incompatible, because fiscal policies are incompatible, that's a side issue. Right now, because we clump all the discussion together, we don't recognize the fact that this policy, which is so tightly integrated across the world, we effectively have one global monetary policy, and because of all this integration we don't spend time.

On the unemployment issue, I guess we didn't spend as much time discussing that primarily because many of us were convinced that, as far as monetary policy could do something, keeping inflation relatively low and stable was probably the best it could contribute to keeping unemployment low. In specific circumstances where they could do more is something we'll be debating for some time, but it is not what the committee focused on.

MR. VELASCO: Could I add one word on the business of whether the IMF is doing the job already so why have yet one more body do the job? I don't quite know, but I would invite you to engage in the following experiment. The world's central bankers and finance ministers will converge upon this lovely city in the next week. They will talk about everything under the sun, and they will talk about things that are very pressing, such as will the European continent still be there in the next few weeks. Maybe there will be a focused and thorough discussion as to whether the overall monetary stance of the world is right or wrong, maybe. If I had to guess, my guess would be no.

Secondly, even if they did have that enlightened discussion, the question is who would know about it. The report is very precise in saying not only do we want a talk shop, we want a report, and reports have a wonderful way of focusing people's minds. If you've got to commit it to paper, then you have to talk about it and you have to worry about what message you're sending. So reports are not simply wasted paper; they're disciplining devices.

Today we have, as far as I know, we have no single regular set of pieces of paper in which the Fed and the ECB and the Bank of England and the Bank of Japan and so on and so forth have to tell the world we think the monetary stance is right or wrong. If we get them to even talk about that and issue this report I think we've gained something, and we need not create a new bureaucracy, we need not create a massive jamboree of five, six, eight central bankers in a room, ventral bankers. I love finance ministers, I used to be one, but this is not for them. If you get them in a room and lock them up for a day or two and have them come up with a report, I think you will have something additional to what we have today.

MR. BEATTIE: To add a personal note on the issue of unemployment, the Federal Reserve actually does have a dual mandate, which is full employment and price stability at the same time. When I covered the Fed I used to ask would you consider other things, at which point every Fed official would blanche and say, "If you send the Federal Reserve Act up to Capitol Hill and open it up again it could come up with anything in it, cotton subsidies, anything." And there's a huge institutional reluctance which I think people have talked about to start debate which may end in a very different position than the one that technocrats would take it.

MR. BRADFORD: Colin Bradford from Brookings and CG. It seems to me there are three subjects here, and you've done very well in covering two of them in the report. My question is whether you need to reconvene on the third one. The three subjects are global price stability or domestic and global price stability, financial stability from a macroeconomic point of view, and financial stability from a regulatory point of view. It seems to me you've done a wonderful job both in writing, as far as I've been able to tell reading it here on the spot as you've been talking, and orally in covering the first two.

My question is really, and I think it's a vital question actually to driving both, as you point out, the domestic institutional aspects of how these problems are addressed. But also the international one is: How do you integrate strengthening national and global financial oversight supervision in regulatory institutions into a framework that is enlarging itself in its view about the relationship between financial stability and price stability? Is it possible that you reconvene yourselves -- am I right, first of all? Is it fair to say you didn't cover in writing at least the regulatory part of this? The regulatory part is actually crucial to the whole, so therefore leaving it out, probably why not reconvene, do a second report and connect the tissue, so to speak? Thank you.

MR. BEATTIE: Would anyone like to volunteer to write a second report?

SPEAKER: I think we are in the process of considering what might form the basis of a second report. It is along the issues not so much of domestic regulation per se but the issues of international spillovers and considering issues of international regulation. This cross-border lending, cross-border spillover of capital flows, how that is learned, what kinds of supervisory arrangements there are for those kinds of things, that seems to me an area that is very much under-researched and under-discussed, and that could potentially be one of the areas we focus on, but I don't think you're wrong in saying we've under- emphasized that particular area.

SPEAKER: Just to clarify, this is not a one-time committee with a one-time report. The committee on international economic and policy reform will probably exist until the international monetary policy committee comes into being, so it could be around for a long time. Our objective, again, was not to range too far. We wanted to focus on one issue. One of the reasons why this group of some central bankers and some finance ministry officials came to talk about monetary policy was because we felt this was one issue where something needed to be put on the table, because monetary policy has become crucial, and there is no framework guiding what central banks are trying to do in practice, so that ended up being the focus of our first report, but it's by no means the last one.

MR. TRINKL: Thank you. Garth Trinkl, Department of Commerce. This is following up a little bit on the previous question. I wanted to know if the three academics on the panel had any comment on the early warning systems that are being developed by the Peterson Institute. They've been under consideration at the Peterson Institute and elsewhere for several years now, about three or four years. And tying this to regulation a macroprudential regulation of national income to public debt and the national income to private debt, we have the dual mandates of inflation and employment. In this multidimensional mandate consideration would this include growth of national income? Would this include growth of national debt and then divide it down between public and private? Thank you.

MR. BEATTIE: Anything you want to respond?

SPEAKER: Quickly, I'm not aware of what the Peterson Institute is doing. I don't know if my fellow panelists are. The problem that I think we saw when I was at the IMF with early warning systems is partly how effective they were, how much in terms of type one and type two errors, and obviously they were very good at signaling past crises but not as good as signaling future ones.

But the other issue is let's say you had a system which you are fairly confident of. Convincing the bodies that need to be convinced that in fact there is a highly probable crisis is really the big issue. We talk as if we had this early warning system, and once it started signaling "red, danger" everybody would react and do what was necessary.

We tend to ignore the very strong political economy in favor of allowing things to be the way they are and not intervening so long as you're not a hundred percent sure that in fact the crisis is going to happen tomorrow. There's always a tendency to kick the ball down the road to avoid taking action, and that to my mind is the bigger issue rather than whether we have enough signs out there that action needs to be taken.

MR. BEATTIE: We're nearly at an end, so I'm going to take my prerogative to ask one last extremely unfair question which I'm going to give each of the panelists 30 seconds to answer, which is: Given what we know now, given all the tools that we now know are available and are making available, what should the Federal Reserve have done differently during the 2000s credit boom?

MR. VELASCO: Well, if you take this framework that we're suggesting seriously, this expanded framework, monetary policy generally and the interest rate in particular should have been not entirely targeted but at least partially targeted toward preventing a movement in asset prices which could later be reversed. I'm saying that almost verbatim because we struggled to come up with a phrase that made everybody happy.

We all know now that there was a bubble in certain asset prices. We all know that a bubble was reversed. We all know that there were some indications ex-ante that that was a bubble. You couldn't be sure, but probabilistically it seemed like a good call, and we're suggesting that in fact if you see that happening monetary policy has a business in worrying about that. In fact, the report is quite dramatic. At some point it says if that means deviating from the kind of output gap that you would be targeting otherwise, so be it. I think that's right.

MR. BEATTIE: So a higher Fed fund rate basically.

SPEAKER: I think there could have been tighter prudential measures. I will say that I remember in report after report of the World Economic Outlook we said that things look fine, but we must remember that financial conditions are extremely accommodative, and there is a risk of what happens when they reverse. But we never proposed any action on that basis. Maybe we should have.

MS. INDRAWATI: I think culmination of monetary restraint and expansion which is less and prudential must be most forceful on the prudential.

MR. BEATTIE: I'm waiting for someone to advocate capital controls. I've not yet heard it.

MR. PRASAD: I certainly won't. I don't think that is the answer. But I think, again, the issue this puts on the table is also an issue that we've been grappling with, which is how to think about global liquidity, because there was a lot of liquidity in the U.S. And in fact, when Raghu and I were at the Fund at the time, we were trying to grapple with this concept of coming up with global liquidity. It's a very loosely defined and unclear term, but it was clear that there was a lot of money sloshing around not just here but because of other countries' policies around the world, and that clearly had some negative implications. Again, we can see the report as an argument for coming up with a better framework to think about those issues.

MR. BEATTIE: With that we're done. I'm sure you all would like to thank the panelists for their time. Thank you so much.

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