The Chiang Mai Initiative Multilateralization (CMIM): If Not Now, then When?

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By Olivia Negus

'New Perspectives on Asia' highlights the research of junior CSIS staff and interns on issues that are quietly shaping the world's most dynamic region.

The U.S. dollar's status as an international reserve currency and safe haven asset means that global financial stability relies, in part, on countries' access to dollars. During economic shocks, investors typically flock to safe assets, causing dollar demand to skyrocket and occasionally creating liquidity shortages, or limited access to dollars, in the process. Liquidity shortages imperil economies across the globe, as the dollar is the most common currency used in cross border transactions. The Chiang Mai Initiative (CMI) was originally founded after the consequences of the 1997 Asian Financial Crisis (AFC) convinced East and Southeast Asian nations that a more robust regional financing arrangement was needed to supplement existing international facilities to avoid the perils of inadequate dollar liquidity. The initiative, which was established in 2000 by the ten Association of Southeast Asian Nations (ASEAN) member-states, plus China, Japan, and South Korea (ASEAN+3), expanded the already existing ASEAN Swap Arrangement to facilitate bilateral currency swaps among all ASEAN+3 countries. Theoretically, such an arrangement would address dollar liquidity needs by allowing CMI members to swap local currency for U.S. dollars when necessary.

With members recognizing a need for further development of the initiative, CMI went through a number of iterations following its establishment. In the wake of the Global Financial Crisis (GFC), CMI was "multilateralized" in 2010 to create the Chiang Mai Initiative Multilateralization (CMIM), a single pooled reserve scheme. In 2014, the total size of the facility was doubled to $240 billion and the IMF "delinked" portion, referring to the maximum amount members could access without IMF co-financing and conditionality, was increased to 30 percent. Most recently, in June 2020 an amended version of the agreement which promises to promote consistency between CMIM-IMF co-financing arrangements, strengthen CMIM-IMF coordination mechanisms, and clarify certain conditionality-related legal ambiguities came into effect. However, despite the ongoing reform and evolution of CMIM, the facility has not been used to-date. Now, the Covid-19 pandemic has caused severe economic disruption and unprecedented GDP contractions across the globe, including in many Asian countries that were growing rapidly before the outbreak. Yet, CMIM funding still has not been activated. Why?

When Covid-19 cases began rising in the United States and Europe in March 2020, financial markets quickly showed signs of escalating dollar demand: oil and stock prices plummeted, and there were record capital outflows from emerging markets. The value of the dollar soared, and markets braced for a liquidity crunch. Without intervention, global financial markets certainly would have been pushed to the brink. Economies with large dollar funding needs did find support, however it did not come from CMIM.

Instead, the U.S. Federal Reserve provided a number of different support facilities to ease the dollar shortage and prevent further financial market turbulence. It purchased a record number of U.S. government bonds, expanded its already existing bilateral swap lines to include a total of 14 central banks (3 of which went to CMIM members: Japan, Singapore, and South Korea), and created a temporary Foreign and International Monetary Authorities (FIMA) repo facility for countries to borrow dollars against their U.S. Treasury holdings. The IMF also created a new Short-term Liquidity Line (SLL) tool for members facing liquidity shortages and has made more than $45 billion available to three countries since the beginning of the crisis through their Flexible Credit Line (FCL) instrument, a facility designed to help mitigate current and future balance of payments pressures. Both these instruments have no ex-post conditionality requirements. In addition, ultra-accommodative monetary conditions created by the advanced economy central banks have resulted in an environment where many emerging markets can issue debt to meet their funding needs, reducing potential demand for CMIM resources.

Now, compared to March 2020, the global financial system has returned to relative stability. According to international reserve and currency liquidity data compiled by the IMF, for all CMIM members in their database, international reserves have since returned to roughly pre-pandemic levels or exceeded them as of June 2020 following an initial drop in the period from February 2020 to March 2020. Ironically, the success of alternative sources of dollar funding raises questions about CMIM's function, while the market-calming ability of dollar swap lines during the financial chaos of the Covid-19 pandemic seemingly proves why CMIM is a good idea.

Here, some of the familiar criticisms of CMIM could explain the lack of use: overall funding amounts are too low, the legacy of IMF stigma is too much of a hurdle to overcome, and the funding application process is too complicated. Nonetheless, only three members of CMIM have access to a Fed swap line, the Fed FIMA repo facility charges a premium often greater than market interest rates and its use is limited to the country's holdings of U.S. Treasuries, and the IMF precautionary instruments have relatively stringent ex-ante qualification requirements. Conditions within the global funding market have recently been favorable towards emerging market countries, but there is still the possibility that they could also turn. Even if CMIM is not perfect, neither are any of the other options. All this begs the question of CMIM members: if not now, then when? If CMIM is not called upon during a global pandemic, will it ever be?

Olivia Negus is an MA candidate at the Johns Hopkins School of Advanced International Studies (SAIS) and a research intern with the CSIS Economics Program.

Tags

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Center for Strategic and International Studies
1616 Rhode Island Avenue, NW
Washington, DC 20036

Tel: 202.887.0200
Fax: 202.775.3199

MEDIA INQUIRIES

H. Andrew Schwartz

Chief Communications Officer

202.775.3242

aschwartz@csis.org

Paige Montfort

Media Relations Manager, External Relations

202.775.3173

pmontfort@csis.org