Economic Aspects of the Irish Exchange Control Regime

R. Kelleher and Colm McCarthy

Special Article

in

QUARTERLY
ECONOMIC
COMMENTARY

April 1980

J. DURKAN
B. O'LOUGHLIN

ECONOMIC ASPECTS OF THE IRISH EXCHANGE CONTROL REGIME

by

ROBERT KELLEHER and COLM McCARTHY

1. *Introduction*

From the foundation of the State until March 1979, the Irish currency was maintained in a fixed one-to-one parity with the pound sterling. Aside from the 50% deposit requirement on capital inflows through the banking system imposed by the Central Bank in recent years, there were no significant restrictions on the movement of funds between Ireland and the sterling area. Capital movements between Ireland and non-sterling countries were subject to exchange control regulations broadly similar to the UK's own, although in practice they were administered in a somewhat more liberal fashion. The Irish controls could be seen as, in effect, part of the price of our membership of the sterling zone, since the UK's own controls would have been circumvented very readily if Ireland had presented an uncontrolled "window" to the rest of the world. So purchases of financial assets in non-sterling countries had to be financed through the dollar premium pool or through foreign currency loans.

In December 1978, in anticipation of Irish entry to the European Monetary System, the exchange controls were extended to the United Kingdom, which had decided not to join the system. Further Irish investments in foreign currency securities were prohibited and holders of bank accounts in the UK were required to repatriate these funds unless the Central Bank permitted them to do otherwise. Existing holders of foreign securities could continue to maintain such holdings and, from October 1979, could, on the sale of such securities, re-invest the proceeds in any country abroad.

The Irish controls are described in detail in the manual issued, and updated periodically, by the Central Bank. A brief account of the main features is given in the Appendix.

During 1979, a relaxation of the controls was announced which permitted life assurance companies and pension funds to invest in foreign currency securities up to the point where their foreign holdings reached 10% of net actuarial liabilities.

The authors would like to thank, without implicating them, all those who were kind enough to comment on earlier drafts, including (5).

Nearly all countries operate exchange control systems of one kind or another. Some countries, particularly less developed, third world countries and those in the Eastern bloc, operate, in peacetime, controls on current as well as on capital account movements. As a result, some of their currencies are effectively inconvertible for any purpose. In wartime, resort to exchange controls is almost universal and amounts to a system of import rationing when applied to the current account. Indeed, the UK exchange controls, abolished in October 1979, originated in World War II. Extending from monetary union at the liberal end to currency inconvertibility in centrally planned economies, there is a spectrum of possible exchange control regimes from which a country can choose. The choice, for an economy heavily engaged in external trade and finance, is an important element in its overall macroeconomic policy.

Prior to December 1978, the Irish exchange control regime involved no controls on current account movements and no significant controls on capital account movements to the UK. Given the dominance of the UK in Ireland's external financial relations, Ireland, in so far as protection of the reserves was concerned, might as well have had no exchange controls at all. Moreover, given the unhindered access to UK financial markets, the Irish private sector enjoyed considerable freedom of action in its external financial dealings. The policy currently in force, however, is one of severe controls on the outward movement of capital by residents. So there has been a sharp movement along the spectrum of exchange control regimes. This may appear paradoxical in two respects. It accompanied our entry into a system of exchange-rate links designed as a step toward capital market integration in Europe. Meanwhile, the United Kingdom, which had previously operated a highly restrictive exchange control regime, now has one of the most liberal regimes in the world.

Since the introduction of the new Irish system of exchange controls there has been very little public discussion of their economic impact and our purpose in this paper is to make a start in that direction. In the next section, we attempt to place exchange control policy in context, as just one instrument of overall macroeconomic policy. Since most popular rationalisations of exchange controls concentrate on their effects on the level of external reserves and on the exchange rate, we begin by considering their rôle, along with the roles of fiscal and monetary policy, under fixed and flexible exchange rate regimes.

We then go on to consider whether controls may have beneficial effects on other economic policy objectives, such as the promotion of employment or the expansion of the capital stock. This is followed by an examination of the various costs of exchange controls. These include direct administrative costs in both the public and private sectors, allocative and distributive effects arising from portfolio disequilibrium and the costs of factors of production used up in avoiding or evading the controls. The paper concludes

with some observations about the appropriateness of the existing exchange control system in Ireland. Exchange control is but one of the issues raised by our EMS entry. We ignore the broader issues here — a recent discussion will be found in (9).

2. *The Macroeconomics of Exchange Controls*

The model of the economy which underlies the analysis of the macroeconomic effects of exchange controls is the standard small open economy model. This model has enjoyed increasing popularity in the study of Irish macroeconomic policy in recent years.

Small open economies are likely to behave as price takers in international goods and capital markets. Unless non-traded goods are a large part of total output, under fixed exchange rates the rate of price inflation will be determined externally. If there is free mobility of capital, the same will be true of interest rates.

Macro policy operates under particular constraints in this system. Money creation derives from two main sources — changes in the level of domestic credit and changes in the net external asset position of the banking system as a whole. If the domestic creation of money falls short of the demand for money, the deficit is made up by capital flows which ensure an overall balance of payments surplus, i.e. an increase in the foreign exchange reserves. The monetary authority is unable to control the money stock in this theoretical model. Changes in the level of domestic credit, which *can* be brought about by the monetary authority, will have no impact on the level of demand nor on the rates of interest or inflation, but rather on the external reserves.

In the real world, however, neither the goods nor the capital markets are as perfect as is assumed in the theoretical model. In particular, restrictions on certain types of personal lending by the banking system, and on personal instalment credit, are unlikely to be replaced immediately by alternative sources of finance in international capital markets. Thus, certain types of credit policy could have real effects, at least in the short run, on the level of consumer expenditure. But prior to the imposition of exchange controls, it was generally agreed that the degree of integration between UK and Irish financial markets was so close that these real effects were not significant in the aggregate — see Browne and O'Connell (1). Thus, monetary policy operated very much as suggested by the theoretical model.

Although in this model monetary policy has no impact on the major aggregates, such as the level of interest rates, the rate of inflation or the level of real economic activity, it does have an important effect on the level of external reserves.

In the fixed-exchange rate, small open economy model, the target level of foreign exchange reserves can be attained by the pursuit of an appropriate policy in regard to domestic credit expansion, without affecting any other important aggregate in the system. Thus, any reserves objective implied in

the introduction of the controls could equally well have been pursued by an appropriate monetary policy without any other macroeconomic implications, and without any of the costs and distortions associated with exchange control. It is on their presumed ability to protect the reserves in the face of capital outflows that most rationalisations of the controls rest.

A reasonably stable overall demand for money is a lynchpin of the monetary approach to the balance of payments. If the demand for money function is unstable, speculative flows of funds could be so large as to require unacceptable shifts in credit policy to protect the reserves. Of course, reserves could be temporarily propped up by recourse to the IMF or to the international capital market, but it would obviously help the argument for exchange controls if serious instability in money demand could be established. In a further study, Browne and O'Connell (2) conclude, on the basis of extensive econometric tests, that the demand function for broad money in Ireland is, in fact, stable, and they go on to interpret this finding as support for the applicability of the monetary approach to the balance of payments to Irish circumstances.

Moreover, casual observation suggests that operators in financial markets have become increasingly well versed in monetary economics. The onset of generalised floating has made the foreign exchange markets riskier and there is a tendency for operators to avoid substantial exposures to currencies unless they perceive basic inconsistencies between a country's macroeconomic policies and its exchange rate position. If this continues, and if operators can perceive policy inconsistencies accurately, speculative flows will tend to reinforce "genuine" flows and will not be an independent source of arbitrary fluctuations in the foreign exchange reserves.

The efficacy of fiscal policy is also limited in a small open economy. While the "crowding out" effects associated with large and relatively closed economies are of less importance, the openness of the economy assures that fiscal stimuli may leak away through the balance of payments and have only a limited impact on domestic output and employment — see McCarthy (7), (8). In the limit, with the economy operating at full capacity, the fiscal policy multiplier may go to zero. We exclude this possibility in what follows, preferring to assume that, in the short-run, activity responds to a demand expansion.

How do we introduce exchange controls into the analysis? Conceptually, the easiest way to do so is to assume that the authorities introduce such controls as enable them to determine the level of capital flows exogenously. The domestic capital markets are now no longer fully integrated with their international counterparts and domestic interest rates, the fixed exchange rate notwithstanding, can diverge from world rates. We are making some polar assumptions here — the controls are across the board, affecting all inflows and outflows, and there is no evasion.

If the authorities now engineer, say, a reduction in the net capital

outflow, reserves and the money supply both rise; interest rates must fall and domestic demand will rise, resulting in an increased level of economic activity but a worsening of the balance of payments on current account. The process continues until activity has expanded sufficiently, and interest rates have fallen enough, to worsen the current account in an amount equal to the initial reduction in the net capital outflow. The reserves will stabilise and so will money supply.

At first blush, it might appear that the authorities have done rather well, increasing the level of economic activity and, thus, accommodating an increased demand for money at a higher level of the external reserves. The extent to which they can continue with the policy is limited by the size of initial capital outflows and the lower limits on interest rates — if you wish, on the supply schedule of foreign funds. As is well known, this latter consideration is also important in regard to traditional fiscal policy. An increase in government expenditure will raise demand, hence imports and hence the current account balance of payments deficit. But the demand for money is higher so reserves rise, capital inflows making up the difference. The fiscal expansion is not always feasible — the process stops when the supply of foreign funds ceases to be elastic at the (in this case) given interest rate. The main difference between the two policies, in qualitative terms, is that fiscal expansion does not move the interest rate from the world level, while exchange controls, where they are effective, will do so. Such a movement is not necessarily desirable.

The manner in which we have introduced exchange controls into the analysis thus far does not correspond to the exchange control regime operated at present by the Irish authorities. The controls do not apply to all capital flows: there are no restrictions on inflows and the controls on outflows apply only to Irish residents. There are no regulations preventing leading and lagging through the current account. Thus, the Irish capital market is far from perfectly insulated from overseas markets. But the qualitative impact of the controls should be the same as in the analysis just given, even if their quantitative importance is reduced by limitations in coverage and by avoidance and evasion.

The break with sterling has altered the framework of Irish macroeconomic policy in certain ways, but we are still participating in a pegged exchange rate system, considering the small margin of fluctuation within the EMS parity grid.

The policy environment changes for a small open economy if it adopts a policy of flexible exchange rates. In particular, monetary expansion can now have only one source, domestic credit expansion, and can, therefore, be controlled by the monetary authority. Price inflation will no longer be entirely externally determined, even though the economy is still a price taker on world markets. Changes in the exchange rate, reflecting mainly domestic monetary policy actions, will now translate the prevailing external rate of inflation into an endogenous domestic rate.

There is less agreement amongst commentators on the efficacy of monetary and fiscal policies in this environment than in the fixed exchange rate case — see the discussions in (3), (6), (10) and (11). However, it is plausible that monetary policy will have its main impact on the exchange rate and the price level, with limited real effects working through changes in asset values. Fiscal expansion, unless the economy is fully employed, will raise demand and activity and, hence, the demand for money. This, with reserves frozen, can have the apparently anomolous effect of appreciating the exchange rate, but this is really no more anomolous than the impact of fiscal expansion on reserves in the fixed exchange rate case.

What happens when exchange controls are introduced? We are now starting from a position where capital flows precisely offset the current account balance of payments deficit. The impact effect of exchange controls will be to create an incipient overall balance of payments surplus which puts upward pressure on the exchange rate. This, in turn, reduces prices and consequently the demand for money. This reduces interest rates and expands the level of activity until the balance of payments deficit on current account rises sufficiently to offset the increased capital flows.

The effects of exchange controls under flexible exchange rates are not dissimilar to what happens in the fixed exchange rate case. In particular, the impacts which exchange controls can have on macroeconomic magnitudes could equally well be achieved by the appropriate choice of fiscal and monetary policies.

3. *Further Economic Impacts of Exchange Controls*

The notion that attempts to increase the stock of financial assets in a country are economically desirable goes back at least to the mercantilists and has appeared in the Irish debate on economic policy under such guises as the periodic calls to "repatriate" the external reserves documented in Fanning (4).

It is difficult to see how objectives, such as the expansion of the capital stock or the promotion of employment, are rendered any easier of attainment through the introduction of exchange controls. Even if domestic residents increased investment, in response to reduced borrowing rates consequent on the controls, unless the marginal efficiency of capital had been increased, something which controls do nothing to encourage, the resulting level of investment would be above the social optimim. But in a country dependent on external finance for investment, things might not work out like this at all.

The attractiveness of Ireland as an investment location to a multinational company depends on the expected real rate of return on Irish versus alternative investments, which is not directly affected by exchange controls at all.

The supply schedule of foreign funds could be shifted in an adverse

direction if foreign investors feared further extensions of controls, limiting their freedom to liquidate investments and to repatriate profits. But this is hardly likely to be a problem in the Irish case, given our commitments on capital movements under obligations to the IMF, OECD and EEC.

As to employment, there can be no doubt that exchange controls create jobs. Whether this is a sensible way to do so is another matter. In the Central Bank, as well as in the commercial banks and in private business, considerable numbers of additional staff are now employed as a result of exchange controls. Precise information is not available, but estimates of the numbers involved run to several hundred. The creation of employment, whether in the public or in the private sector, which results in no increased output of useful goods and services, is essentially redistributive rather than productive, and, in our view, has little to recommend it as an element in employment policy. It is sometimes argued that fully effective exchange controls could, through insulating the domestic financial markets totally from outside influence, render monetary policy effective for economic stabilisation, even under fixed exchange rates. The possibility seems remote under the present Irish arrangements, however: the controls are limited in coverage and their effectiveness presumably less than total. To create a role for monetary policy in a fixed exchange rate open economy of similar importance to its role in a closed economy would virtually require the abandonment of convertibility. In any event, monetary policy autonomy is not an end in itself and the availability of alternative stabilisation policy instruments must place a strict limit on the price one would be willing to pay for it.

4. *The Costs of Exchange Controls*

a. Direct Resource Costs

The direct costs of exchange controls are the opportunity costs of the factors of production tied up in operating the system. The authorities bear some of these costs but the major proportion is presumably borne by business. As well as factor costs, there are delays in form-filling and processing through banks or authorised agents before "genuine" movements of funds are sanctioned by the Central Bank. These costs are difficult to quantify in the absence of a comprehensive survey of commerce and industry. But they can hardly be trivial, given the extent of the controls and the size of Ireland's foreign trade.

Prior to the break with sterling, almost one-half of Ireland's external trade in goods and services and an even larger proportion of Ireland's external financial dealings, representing the UK's share in these areas, could be conducted as easily, for practical purposes, as if they were internal deals in Irish pounds. Exchange control costs, in addition to the (unavoidable, given the end of the sterling link) costs of currency conversion must now be incurred in respect of all overseas transactions on both current and capital account.

In addition to the direct costs of operating the system of exchange controls, there are hidden costs in the form of the resources devoted to avoidance and evasion. It has been argued that the effectiveness of any exchange control regime depends on the willingness and ability of the authorities to tighten the regulations at as fast a rate as the private sector discovers new loopholes.

b. Allocative and Distributional Costs

Exchange controls of their very nature must impose costs on the owners of asset portfolios, since the essence of exchange controls of the type Ireland has adopted is to intervene in the asset-selection decisions of these portfolio owners.

Under fixed exchange rates, the immediate impact of the controls is to re-allocate the community's holdings of foreign assets away from the private sector and into the official external reserves. If there is any tendency for the return earned on official foreign asset holdings to be lower than would be obtained by the private sector, there is a loss of foreign earnings to the community. Given that Central Banks tend to hold short-dated, or completely liquid, assets, which usually yield lower returns, and given the conservative approach which they normally adopt to portfolio management, such a tendency is probable.

However, the increase in external reserves is less than the reduction in foreign holdings of the private sector, due to the increased balance of payments deficit on current account. Overall holdings of foreign assets are reduced, but the reduction in borrowing rates discussed earlier will see an increase in domestic investment expenditure. The re-allocation of the community's total capital portfolio from foreign to domestic assets will reduce the total income flow from these assets, since lower-yielding domestic assets have been substituted for the foreign ones.

In a world of competitive markets, investment expenditure is undertaken up to the point where the marginal efficiency of investment equals the opportunity cost of capital. If social and private returns are equal, this results in a socially optimal level of the capital stock. The social opportunity cost of capital is the world market rate of return. By depressing domestic yields below this point, exchange controls will result in a level for the capital stock that is not the social optimum.

It can immediately be objected that we do not live in a world of perfectly competitive markets. All sorts of externalities and distortions serve to ensure that social and private returns do, in fact, diverge. However, if exchange controls of the Irish type were to be a possible remedy, it would be necessary to prove that the net effect of the distortions was such as to hold domestic investment below the social optimum — otherwise, controls on outflows would exacerbate the problem. Moreover, the distortions would have to affect international, relative to domestic, capital, and not just

the overall attractiveness of investment. Even if these conditions could be shown to hold, remedies other than exchange controls could be the most suitable.

The reduction in domestic yields, brought about by the introduction of effective exchange controls, will cause a redistribution from savers to borrowers. Some of the benefit goes to the public sector in the form of increased profits for the Central Bank — the increase in the reserves will be held in the form of interest-bearing assets, matched, at least to some extent, by non-interest-bearing currency liabilities. One wonders whether a redistribution from savers to borrowers is deemed desirable in its own right by the authorities.

The Irish economy is characterised by large-scale public and foreign ownership of the industrial capital stock. As a result, the market capitalisation of Irish equities (some of the largest quoted companies being in the financial sector to boot) is only about £900m. This is a far smaller proportion of the nation's capital stock than is represented by quoted securities in other countries. Domestic financial institutions which wish to hold equities in their portfolios must, in practice, seek most of them abroad in these circumstances. While many institutions will, for prudential reasons, wish to match their, mainly domestic, liabilities with assets of the same currency denomination, it remains the case that any given system of restrictions on outward portfolio investment would be less of a burden in a country with a more developed equity market.

There is a prohibition on the transacting of forward exchange rate cover for deals not related to trade. Since forward rates reflect interest rate differentials, portfolio investors can get exposure in overseas markets, through local financing, at costs which can differ very little from those which would prevail in the absence of this regulation. But it must discourage Irish business from borrowing abroad, through preventing the off-loading of currency risk, and to that extent is likely to increase the severity for the private sector of any given degree of quantitative credit restriction.

5. *The Effectiveness of the Irish Controls*

It is always difficult to quantify the extent to which evasion can frustrate the effectiveness of an exchange control system. This is not so much a problem with avoidance, i.e., with legitimate methods of effecting capital flows.

Non-residents are not subject to the Irish exchange control restrictions. Data on asset-ownership by residence are poor. However, it is probable that total non-resident ownership of fairly liquid assets (deposits, gilts and quoted equities) would be of the same order of magnitude (£1,000m.) as the foreign exchange reserves. The liquidation of these assets could not be prevented at all. It is possible that the introduction of controls might see foreign portfolio investors squeezed out by domestic investors at the margin, with a reduction in the extent in which portfolios are diversified internationally.

Moreover, there are no controls on the current account of the balance of payments, so currency speculation could take the form of accelerating or delaying payments for imports and exports. This "leading and lagging" is of great potential importance in a country with such a large external trading involvement as Ireland. The total of Ireland's imports and exports for 1980 is forecast at above £10bn. If a one-month delay in the realisation of export receipts coincided with a one-month acceleration of import payments, external reserves would almost be wiped out. Finally, residents who are subject to strict controls on capital exports can always attempt to evade them.

In the course of his opening statement in the debate on interest rates in Dail Eireann on Wednesday, April 16th, 1980, the Minister for Finance remarked:

> "This is an appropriate point to mention the exchange controls, which, though they afford a degree of protection, cannot insulate us from external influences. Exchange controls relate to capital movements. Leads and lags in relation to payment for our trade, even in relation to one month's transactions could, on their own, exceed the total level of official external reserves.
>
> As regards financial transactions, exchange controls do not and cannot relate to non-residents who have large balances and holdings of financial and other assets within the State, all of which could be run down at their wish.
>
> As regards residents, they have large liabilities to abroad and could run them down without being restricted by exchange control, which must allow residents to pay their debts abroad. In addition, exchange control cannot force residents to borrow abroad and it may very well be that, as in this year, we need the private sector as well as the Government to effect significant capital inflows."

It is difficult to avoid the conclusion that, in the event of serious downward pressure on the exchange rate, the Irish system of exchange controls would be of strictly limited effectiveness in conserving the official holdings of foreign exchange.

Through the intervention arrangements of the European Monetary System, Ireland now has access to, in principle, unlimited foreign exchange support from its partner-states, in addition to its entitlements to drawings from the International Monetary Fund. So the wherewithal to resist what the authorities believed to be an ill-founded speculative raid is already available. One of the lessons of the postwar experience with fixed exchange rate systems is that resistance to what one believes to be well-founded speculation is both expensive and, ultimately, pointless.

The present Irish system of exchange controls dates from the period of transition from membership of the sterling area to a new exchange rate regime. That transition has now been accomplished and the issue we wish to raise in this article is whether or not we should continue with the controls now in force.

If monetary and fiscal policies can be geared to consistency with the exchange rate target, there should be no need for exchange controls. In the event that perfect consistency is not attained, and of course it never will be, fluctuations in the reserves will result. But that is their function, and is the principal reason for holding them in the first instance.

With monetary and fiscal policies which are not consistent with the exchange rate, it is extremely doubtful if exchange controls can do any more than postpone the day of reckoning. These controls are costly to operate and do not appear to generate any indirect benefits.

In these circumstances, we conclude that exchange control should not be a permanent feature of Irish macroeconomic policy.

APPENDIX

(The following account of the Irish Exchange Control arrangements is taken from the OECD Economic Survey of Ireland, August 1979, Annex 1. Note that the UK's exchange controls have since been abolished, so there is no longer an investment currency market.)

System prior to 18th December 1978

Prior to 18th December 1978, Ireland and the United Kingdom (for exchange control purposes, Northern Ireland, Great Britain, the Channel Islands, the Isle of Man and Gibralter) operated broadly similar exchange controls vis-à-vis residents of third countries (termed non-residents) while, in general, maintaining complete freedom of capital movements between each other's residents. The Irish controls were, however, somewhat more liberal in a number of respects than their United Kingdom counterparts.

In brief, trade and other current transactions (including travel) and outward direct investment in and personal capital movements to other EEC member states, were subjected only to supervisory controls. These controls were applied solely for the purpose of ensuring the bona fides of the transactions concerned. Allowances were available for personal capital movements outside the EEC, while outward direct investment transactions outside the EEC were dealt with on their merits. Outward portfolio investment was allowed through the medium of the investment currency market. The investment currency market operated as a medium through which Irish residents could buy foreign currency to invest in foreign securities from other Irish or U.K. resident sellers of such securities. The currency, in general, sold at a substantial premium over the official rate of exchange. The currency was also available for outward direct investment transactions in and personal capital movements to countries outside the EEC in excess of the basic allowances available. Irish residents were not allowed to retain foreign currency on deposit or lend Irish pounds to non-residents except with the permission of the Central Bank. There were, in general, no exchange controls on capital inflows.

Changes introduced with effect from 18th December 1978

On 15th December 1978, in light of Ireland's prospective membership of the EMS, exchange controls were applied for the first time to transactions by Irish residents with residents of the United Kingdom. The controls were intended to limit the possibility of disruptive capital movements emerging in the context of Irish membership of the EMS. Broadly speaking, the controls now applied to transactions with residents of the United Kingdom are the same as had already applied to transactions with other EEC member states.

The system as it now stands includes a number of additional changes made in January 1979. Thus, although Irish resident holders may continue to switch holdings of foreign securities eligible for sale in the investment currency market, they may not buy additional investment currency. Investment currency is no longer available, therefore, for the purchase of additional foreign securities or for outward direct investment transactions in or personal capital movements to countries outside the EEC. Irish residents have also been required to repatriate bank balances in the United Kingdom, unless permission to retain them has been obtained. Furthermore, a number of supervisory controls on capital inflows have been introduced, but there are no restrictions on such inflows.

As the United Kingdom has not applied exchange controls to transactions with Ireland, existing arrangements to ensure that Ireland is not used as a channel to evade United Kingdom controls continue to apply.

Controls now operating

There are no restrictions on current trading or invisible transactions. Apart from small transactions, however, foreign currency for payments must be obtained through the authorised banks. Export proceeds must be repatriated without delay.

Personal capital movements to EEC member states are only subject to supervisory controls. Allowances are available in respect of most personal capital movements outside the EEC. The purchase of personal property outside the EEC may be financed with borrowed foreign currency repayable with official exchange in instalments over five years.

Outward direct investment in the EEC is also only subject to supervisory control. Outward direct investment projects in other countries are dealt with on their merits. In general, an appropriate amount of the financing of approved projects is with foreign currency borrowing. Inward direct investment is supervised but there are no restrictions.

Apart from investment by institutions with borrowed foreign currency no new outward portfolio investment in foreign securities is allowed. Existing holdings of such securities may, however, be retained and may, subject to certain conditions, be switched for similar securities. Such securities may also be sold to non-residents and the proceeds repatriated.

There are no restrictions on inward portfolio investment. Payment for Irish securities purchased by non-residents must be in foreign currency or its equivalent. Transactions above a certain value are supervised.

Irish residents may borrow foreign currency from authorised banks for direct financing of trade. Central Bank approval is required for non-trade foreign currency borrowing but is generally granted for productive purposes. Except in some minor cases, authorised banks are not allowed to lend Irish pounds to non-residents without Central Bank approval.

Irish residents may not hold foreign currency accounts except with the permission of the Central Bank. Permission is generally given where accounts are required for commercial or, in certain cases, personal reasons. There are no restrictions on inflows into non-resident Irish pound accounts. However, for supervisory purposes, credits to such accounts above certain values require permission. Furthermore, the open positions of banks in foreign currencies are controlled in certain respects.

Authorised banks may provide forward cover to residents and to non-resident banks for transactions directly related to the movement of goods and related services between Ireland and any other country, subject to documentary evidence being obtained for each transaction. The provision of forward cover is also subject to conditions relating to the timing and amount of transactions.

Administration of exchange control

Day to day administration of exchange control is carried out by the Central Bank of Ireland which acts under delegated authority from the Minister for Finance. The Central Bank, in turn, has delegated authority to authorised banks, and to a lesser extent, approved agents (stockbrokers, travel agents, etc.) to approve most current and some capital payments.

References:

1. Browne, F. and T. O'Connell: "A Quantitative Analysis of the Degree of Integration between Irish and UK Financial Markets", *Economic and Social Review,* 9, 1978.
2. Browne, F. and T. O'Connell: "The Demand for Money Function in Ireland: Estimation and Stability", *Economic and Social Review,* 9, 1978.
3. Casas, F.: "The Short-Run Efficacy of Monetary Policy Under Floating Exchange Rates Reconsidered", *Journal of International Economics,* 8, 1978.
4. Fanning, R.: *The Irish Department of Finance 1922-58,* Dublin: Institute of Public Administration, 1978.
5. Kelleher, R.: "Some Economic Aspects of Exchange Controls", mimeo, October 1979.
6. Kelleher, R. and C. McCarthy: "Flexible Exchange Rates and Stabilisation Policy in a Small Open Economy", Central Bank of Ireland Paper No. 1/RT/78, January 1978.
7. McCarthy, C.: "Economic Development and Economic Policy", *Administration,* 27, 1979.
8. McCarthy, C.: "The Impact of Job Creation on Unemployment and Emigration", *Central Bank of Ireland Quarterly Bulletin,* Summer 1979.
9. McCarthy, C.: "EMS and the End of Ireland's Sterling Link", *Lloyds Bank Review,* April 1980.
10. Niehans, J.: "Some Doubts about the Efficacy of Monetary Policy under Flexible Exchange Rates", *Journal of International Economics,* 5, 1975.
11. Turnovsky, S. and G. Kingston: "Monetary and Fiscal Policies Under Flexible Exchange Rates and Perfect Myopic Foresight in an Inflationary World", *Scandinavian Journal of Economics,* 79, 1977.