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Review paper

TOBIN TAX - REDUCING THE NEGATIVE EFFECTS OF CAPITAL CONTROLS AND SHORT-TERM CAPITAL MOVEMENTS

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Abstract

The phenomenon liberalization, with the influence of the Bretton Woods system that collapsed subsequent to the Oil Shock in 1970, first began with the efforts to discover markets to value the investments of these countries in the developed countries. In order to provide the desired capital figures, in the 1980s the developed countries, squeezed under the debt load together with insufficient capital accumulation and low saving rates, needed the foreign resources and, at this point, the liberalization process of capital gained importance. Realizing the growth and developmental targets of countries' economies, their integration in the liberalization gained great importance.

The developing countries' integration in the system without the necessary arrangement in their financial structures had an effect in terms of disturbing the stability of the economies, particularly in short-term capital inflows. As much as the problem created by the speculative capital inflow, the immediate outflow of this capital, disturbing the balance of economies, also caused crisis.

To minimize the negative influence of short-term capital, capital controls are emphasized. Just as these controls can have various application ways, the most emphasized and discussed application was Tobin tax. Even though there are various disagreements in terms of whether or not Tobin tax affected the capital inflows, the examples of Malaysia and Chile represent successful results.

In the first section of this study, the development of the liberalization process will

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be examined. In the second section, the effects created by the capital movements, and particularly short-term capital movements, on the countries' economies will be emphasized. In the third section, the capital controls and Tobin tax, suggested for reducing the negative effects of the short-term capital movements will be considered and the applicability and limitations of Tobin tax will be examined.

Keywords: *Liberalization, Capital control, Tobin tax, long termed capital movements*

JEL Classification: G10, E66, F38, O40, J10, H29

Introduction

Together with the Second World War, the countries adopting the principle of capital controls of the Breton Woods System, also with the effect of the Oil shock in 1971, following the collapse of the system and emergence of stagflation tendencies, started the applications in the direction of removing capital controls. This situation caused the globalization movement to accelerate and thus form the liberalization process. In this period, the economic depression and debt crisis in developed countries cause these countries to adopt the financial liberalization to overcome the recession, also with the effect of the financial agencies such as IMF and World Bank (Kara and Kar, 2005:96). With the liberalization policies applied, firstly, the limitations on the domestic financial markets were removed, and then, the limitations on the capital movements (Keskin, 2009). By removing the limitations, the countries rapidly integrated in the system, however, the developing countries which integrated in the system did so without making the necessary arrangements in their financial markets, and capital inflows disturbed the stability of economy. Financial capital movements can lead to fluctuations in variables such as the exchange rate used by central banks as main or sub-target, foreign currency reserves, monetary magnitudes, and inflation and make ineffective the monetary policy (Hoggarth and Sterne,1997). While the capital flows going toward the developing countries satisfy the demand for resources, the immediate inflows and outflows of capital increased the vulnerability of countries' economies. In many developing countries in the 1990s, when the financial liberalization movements accelerated, there was a period when the important increases in the international capital movements actualized and also the severe crises were experienced, which emerged in frequent intervals and can spread easily (Bedestenci and Kara, 2004;Işık,2005). The crisis experienced led the policies supporting the marketization of economies to be reasoned and the views supporting the necessity of the alternative policy applications to emerge (Ay and Mangır, 2007).

The major alternative policy applications are the capital controls. In terms of effectiveness of capital controls, there is no consensus in the literature. According to the economists which view capital controls as positive, if due to speculative attack, a problem in the balance of foreign payment is encountered and the existing arrangements cannot cope with this problem, appealing to the capital control may be a solution. In this sense, the examples of Malaysia and Chile are quite successful. According to the economists emphasizing the negative effects of capital movements, these controls, regarding the structural reforms, because the existing crocked economic relationships to last. In addition, it is considered that these controls will not be effective via the derivative markets (Ankara Sanayi Odası,2001).

Among the policy applications suggested, the most remarkable one was Tobin tax, put forward by Tobin. This tax, is ad valorem tax, which, in the first studies of Tobin, was brought into the spot of foreign currency buying systems, is considered to be between 0.1% and 0.5 %, and in his next studies, is thought that it can increase up to 1%. (Yılmaz, 2004).

Liberalization Process

Abolition of financial liberalization policies starting throughout the world the control on capital and the developments in the information and communication technologies accompanying the case engendered the result of realization of the capital movement globally (İnandım,2005). Globalization includes liberalization, cleansing the movement of capital crossing the country borders from the governmental system (Kazgan, 2005: 17). Globalization movements generally emerge in two forms: commercial liberalization and financial liberalization. Trade liberalization expresses reduced public intervention; making the government smaller; freedom of foreign trade; privatization applications; elimination of trade barriers, product barriers, regional limitations; and export oriented growth strategy (Seyrek, 2002). It is considered that the export values of outward -oriented economies grow more rapidly and export oriented positive externalities provide the country economy to grow more rapidly (Dollar,1992) According to the financial liberalization in the broad meaning, it is necessary to apply a staggered policy including functional and institutional arrangements. These are the elimination of credit controls; deregulation of interest rates; that there are the in –out freedom to banking sector or, more generally, financial sector; autonomy of banks; and liberalization of the international capital inflows (Williamson and Mahar, 2000:7). In capital markets, among the causes of liberalization, providing the effectiveness in the distribution of resources, development of financial markets, and effect of international organizations can be shown (Özdemir and Sever, 2004). Together with financial liberalization, elimination of controls, preventing the price deviations, ensures that savings go toward the high return investments (Eser, 2012). The interaction on international markets and technological developments caused the financial markets to deepen and this also accelerated liberalization. The liberalizations in exchange rate regime contribute to the markets of developing countries and international financial agencies, but the developing countries limited the possibilities of being able to follow the independent monetary, exchange rate and interest policies and eliminated the possibilities of the countries in question to identify the idiosyncratic growth and development targets (Yeldan, 2002). According to the arguments for financial liberalization, with elimination of capital controls, the savings, orientating to high return area of investments, will be distributed more effectively.

The most important contributions of capital inflows are that they satisfy the financing needs of firms; becoming easier to access credit, they accelerate the consumption expenditures; and, increasing the supply of foreign currency, that they cause to exchange rate to be valued (Toga and Berument, 2011). After the financial liberalization, in the developing countries, whose domestic savings are not enough, the interest rate will rise and the savings of countries that have saving surplus will go toward these countries. While this process causes the interest rates to level in countries, the increase of competition will lead the financial markets to run more effectively and the owners of saving and investors to reach the better possibilities (Ansell and Sungur,2000). Empirical observations, as a result of financial liberalization, show that the interest equality among the countries were not provided (Akyüz, 2003). The main reason for this case is that international capital flows are realized in the way of short=term capital flows (Kaya, 2008). The phenomenon of globalization in the financial markets caused the formation of capital sizes pursuing the arbitrage gain and this capital to flow to the developing countries (Berksoy and Saltoğlu, 1998).

In the early 1970s, in the developing countries, the effectiveness of labor fell and profits declined. This caused both the decrease of investments and fall of the growth figures (Kaya, 1998). From the second half of 1974s, investors, escaping from the real investments, went toward to the financial investments. In the 1980s, developing countries began to experience the difficulties in settling the foreign debt; their macroeconomic balances disturbed; and, in this countries, the interest rates rose. The developing countries instead of borrowing from abroad preferred the foreign direct investments and portfolio investments (Calve et al, 1993; Dooley and Kletzer 1994). However, the foreign capital inflow considered did not became continuous and permanent, after realizing the speculative profit aim, left the relevant countries. In the developing countries, beginning from 1995, important changes occurred in terms of the quality of capital inflows, Until 1995, while the formal capital inflows taking place in the long-term foreign credits was predominant, after 1995, in such a way that it will include the portfolio and direct investments, private capital inflows gained intensity. In the countries, where this capital inflow occurs, both national money over valued and accumulation was experienced in the reserves of foreign currency (Yeldan, 2002). For the developing countries that were in capital trouble, this situation, as “an unproblematic financing resources” in the beginning, with the deflection of capital of interest, the maturity of a large part of which is less than one week, suddenly and in high amounts caused these countries to experience disaster of financial crisis (Gedikli,2010).

In capital movements towards the developing countries, the factors of push and pull become effective. Pull factors, as a result of the changes occurring in the policies of developing countries and developments related to the other foreign expansion, expresses the improvement occurring in the risk characteristics of these countries. Arias and Montiel (1996) summarize the pull factor as follows:

- the improvement in the structural and institutional reforms and macroeconomic policies leading to the increase in the expected long termed return of capital
- short termed macroeconomic policies
- the policies increasing the foreign expansion of domestic finance markets like

eliminations of capital controls or restrictions applied to the direct investments,
- debt-stock swaps, sustainable borrowing, and contracts leading to the decrease in debt stock,
- stabilization programs increasing the effectiveness of resource distribution and structural reforms
- the policies providing the absorption capacity of the domestic economy to increase, compared to income,
- due to some changes occurring in the rates of international trade, variations seen in the national income,
- Institutional management and internal audit (Yazgan and Kayacan)

The factors of push are independently affected from the developments in the developed countries and changes in the regional risk perception of investors. This makes the reversals experienced in the capital flows more difficult to be predicted:
- foreign interest rates and conditions of internal cycle.
- the developments reducing the access cost to the capital markets in the creditor countries.
- the contagion effect in the international capital markers

Sorts of Capital Movements

Global capital movements are indicated as direct investment, short termed monetary capital, central and fiscal funds, interest arbitrage, speculative fund flows, and money laundering.

Foreign trade investment is divided in two groups. First of these are the security areas, termed as portfolio investment, in other words, hot money. The second is the capital brought to increase the production capacity. With these kind of investments, expressed as foreign direct investments, a firm is either established in a foreign country or, investing capital on the company in a foreign country, where the main firm grows. Portfolio investments are short termed. These kinds of investments leave country quickly and deepen the dimension of crisis (Acar, 2003).

When the controls on the capital movements are removed, a capital inflow occurs in the developing countries. The reason for this, the interests rates in the developing countries, rising, go up the average of international rates. Since this also means a profitable investment for the foreign investors, a capital flows toward the developing countries. The relationship between the short-term capital movement and exchange rate keeps an important place in shaping of financial crises. In conditions of floating or free exchange rates or fixed exchange rate, often exposed to variations, it is possible to avoid the risks of exchange rate. If one can avoid the risks of exchange rate, the short termed capital movements do not occur. Because the risks of exchange rate are undertaken consciously, when the short termed capital movement occur, these provide stability or become the element of lack of stability (Kındleberger, 1970).

The capital flows liberalizing in the form of fiscal funds, under pressure from exchange rate fall, provide a higher return to the capital which leaves the country of origin. This capital will create crisis in the country-destination, particularly if it's a developed country, whose financial markets are struggling, and thus speculative movement is emphasized. In order to utilize the short termed interest rate difference that exists between two financial markets, interest arbitrage, expressed as the use of funds in the trade of short termed security, includes very short termed capital movements and portfolio investments, because, institutionally, the differences between international interest rates and domestic interest rates largely leads to short termed capital movements (Işık-Duman-Korkmaz, 2004: 59).

There are three main features of specifications. First is that every ascent has a descend and that ascents conclude a collapse at some point. The second is that there are always losers in the face of winners and, in general, that is that the case, in which no income can be created during speculation. Finally, when the profit rate of capital falls, it is that the speculations gain intensity and that the demands for funds is to be reflected.

Black money is the value of every kind of property, very generally, obtained by committing an offence. The identity and citizenship of funds, which enters and departs in the form of the fluid funds, are not certain. Liberalization of capital movements accelerated the formation of black money. Some part of unrecorded economy is related to the widespread and general applications of the recorded firms such as tax evasion, not paying for the premium of social security, indicating low the number or wage of worker. Some part of it consists of offenses which globalize and in which, a number people participate in, such as arms smuggling, drug trade, terror financing, acquirement of international bid by corrupting, the size of its dimensions made a current issue the obligation of these black money originated funds to find a way absolutely to gain favor and to be laundered and the important role of black money in the financial crisis experienced in the developing countries (Kazgan, 2005).

The effects of liberalization of capital account on the country economies

There are two main effects of liberalization of capital movements on economies; positive and negative. Each of these effects leads to the remarkable changes in the economy. Therefore, the decision to liberalize capital movements must be made by taking into consideration the idiosyncratic dynamics of countries.

Positive Effects

Removal of consumption fluctuation: together with the freedom of access to international capital markets, in the times, when a country's economy is in a bad position, borrowing from abroad and, in good times, lending abroad, the consumption fluctuations are removed. Thus, capital flows increase the economic welfare, bringing the consumptions of household stable.

Domestic investments and growth: according to Prasad et al. (2003), in the developing countries, the positive effects of globalization on the economic growth emerge via various channels. The increase in domestic savings reduces the cost of capital and the technology transfer from the developed countries to the developing countries and the development of domestic financial sector express these channels. As long as marginal return of domestic investments are equal to or more than the cost of capital , net inflows of foreign resources emerge as the extra resources to the domestic savings; increase the amount of physical capital per employee; and thus, help the country, where the capital inflows, increase the economic growth rate and raise the standard of life. This is the view underlying the neoclassic theory. According to the neoclassic theory, the capital must flow from the countries, where marginal efficiency is high, to the poor countries.

Artery, Eichengreen and Wyplosz (2001), as in the other many studies, in the openness degree of capital movement, used the openness index, published by IMF. The authors, in their studies, in the countries that currently provided the commercial liberalization, and in which macroeconomic instability is low, found a positive relationship between capital account openness index and growth.

On the other hand, Edison, Levine, Ricci and Slok (2002), using the data of the period 1980-2000, in the analysis they conducted of 57 countries, came to the conclusion that liberalization of capital accounts was not effective on the growth.

According to Prasad et al.(2003), the results of empirical study point out that the soundness of fiscal structure of the financial institutes, where investment is made, were determinative on the ability to be able to attract the investment and macroeconomic effects of financial liberalization. According to the authors, it is observed that the potent legal structure and supervision on financial arrangements; lowness of corruption degree; transparency and good institutional governance strengthen the positive effects of financial integration. Bosworth and Collins (2000), between the years of 1979 -1995, with panel regression technique which they applied in 58 developing countries, examined the effects of capital flows on the investments and concluded that the effect of FDI on the investments were positive, while portfolio investments did not have a strong influence.

Alfaro, Chanda, Kalemli-Özcan and Sayek (2004), in their studies which include a number of countries which they had examined during the period 1975-1995, suggested that the contribution of FDI, alone, to the economic growth was uncertain; however, that the countries, whose financial markets are developed, became more successful in utilizing from FDI.

Eichengreen (2001) approached the issue from macroeconomic point of view and, especially in the countries having the relatively skilled labor and whose physical infrastructure is developed, emphasized that the flows of private capital increased the effectiveness. Edwards (2001), in the model he applied for 62 countries, especially in the less developed countries, reached the conclusion that there was no remarkable relationship between the financial liberalization and growth.

The increasing macroeconomic discipline: another view, put forward on the capital flows, is that, since financial freedom increased the return of good polices and worsened the results of bad policies, the phenomenon it encouraged the policy makers about applying more disciplined macroeconomic policies (World Economic Outlook, IMF, 2005).

The improvement of the financial system and financial stability effectiveness: in the last period, one of the views argued, increasing in the favor of the financial integration, is the view that the domestic financial markets increased the deepness and the degree of effectiveness of the financial mediation process, since it improved the resource distribution and reduced the investment cost, increasing the profitability emerging in the markets carrying monopolistic (Babaoğlu,2005)

The negative effects of liberalization of capital accounts on the country economies

The ineffective domestic distribution of capital flows. If capital inflows are used to finance the speculative and poor quality domestic investments, its effect on the long- term growth becomes limited. The investments on the sectors, whose productivity is low and that is not relevant to the trade, reducing the export capacity of economy in time, causes the external imbalances to grow. In the book (1997), published by the World Bank, and in which the capital flows, realized by the developing countries, are examined, it is pointed out that the intensive capital inflows can attenuate the portfolio quality of banking system. The reasons for this are the incompatibilities of monetary unit and mature.

Macroeconomic stability loss: one of the most important theses put forward against the financial liberalization is also the view that in the large dimensional capital inflows emerging in this process, leading to excess total demand, rapid monetary expansion, inflationist presses, valuing in the real exchange rate, and the deficits of growing current accounts did not make any contribution to macroeconomic stability environment in the countries; otherwise, feeding the instability, led to the financial crises (Akyüz,1995).

Herd psychology, contingency, and fluctuation of capital flows: in the short-term capital movements, sudden stoppage that can emerge with the speculative press toward the domestic money and the danger of pullback point out that the borrowing countries can face to the high cost cash escapes (Calvo, 2008). According to Chang and Velasco (2000), the higher the rate of the short termed debts of the borrowing country to the international reserves, the higher the possibility of sudden capital outflows is. While Radelet and Sachs (1999), in their studies, also considered the main resource of crisis experienced in the Asian countries as the sudden capital outflows; emphasized that the short-term structure of flows accelerated the outflows and, noted that in almost all countries affected by the crisis, the rate of short-term debt/official reserve was low.

The risks created by the accesses of foreign banks. Agenor (2001) puts in order the risks the access of foreign banks to the market creates.

- The foreign banks, preferring to make loan available to the firms that are large and have a high reliability rather than the small firms and consumers, create a negative effect on the economic output employment, and income distribution.
- Generally, in the face of foreign banks access with the low operational cost, the competitive press on the local banks will increase and, forcing them to merge, [this situation] will lead "the banks too big to bankrupt in the market to emerge.
- The access od foreign banks to the market will not be enough alone, in case of emergence of banking crises, it will lead the enormous bankrupts to emerge.

Capital Controls

Capital controls are the official arrangements affecting the international capital movements (Vergil, 2002). Capital controls, implemented in the extraordinary situations such as 1st World War, Great World Depression, and 2nd World War, following the last war, in both Eastern and many Western counties, together with becoming popular of central economy, it became one of the main instruments of the economic policy (Keskin, 2009). International capital flows enter and go out the national economy through very different ways and the uncertainty and risky environment form an appropriate environment for the capital controls. Against these negative economic effects caused by the capital movements, capital controls are every kind of policies the country applied, in order to limit the transactions of capital account or direct (Neely,1998). The especially remarkable and discussed application in capital controls is Tobin tax.

Magud and Reinhart (2007) define the four fears for capital controls:
- The fear of valuation of exchange rate.
- The fear of "hot currency"
- The fear of high volume capital inlet
- The fear that the independency of monetary policy will be lost

Johnston and Timisoara (1998) put in order the reasons for capital controls as follows.
- Payments balance and macro management
- Market and institutional evolution
- The cautious policies
- The size and openness of economy

Capital controls are emphasized in two ways, directly and indirectly.

In direct capital controls, direct limitations are brought into the capital transactions and payments related to these transactions, and transfer of funds via the apparent prohibitions, quantity limits, and approving mechanisms. The limitations regarding the relevant sort of capital are carried out by imposing on the banking sector (Ariyoshi et al, section 1, box 1, 2000).

Indirect capital controls are preventing the capital inflows by increasing the costs of financial transactions providing the capital movements. They are applied as multiple exchange rate system, open taxation, indirect taxation.

Multiple Exchange Rate System: In dual exchange rate systems, for the transactions of current account such as import and export and for the transactions of capital account forming as a result of capital flows, the different exchange rates are applied. Multiple exchange rate system is generally applied during the crisis of payments balance. While the part of this system running in the way of fixed exchange rate is protecting the trade operations from the movements of exchange rate, its part running in the way of floating exchange rate system, moving according to the supply and demand in the market, provides the economic sectors with flexibility in the applications of monetary policy (Fan, 2004).

Open taxation (Tobin tax) : In this application, it is obligatory for the bank or non-bank financial agencies to hold the foreign currency that equals the determined rate of net exchange position or capital that equals to the domestic currency equivalent of this total in the central bank of country without interest. This kind of control is applied to both capital inflows and capital outflows.

The application difficulties of capital controls can be put in order as follows:

- If the capital coming to country is reported as a sort of capital to that the control are not applied, it means to bypass the relevant controls.
- In the capital control, as the tax rates, time to hold capital, and exception number increase, the complexity of the system also increases.
- It is necessary to continuously update the content of capital control application, in order to prevent bypassing the control; however, this situation increases the costs of applications (Kokenyne et al, 2010).

Since capital control significantly affected the system, it causes the financial system to slow during application. Capital controls are used as an instrument in preventing the financial crises. For preventing the formation of crises, different polices are also applied.

The policies applied for preventing the emergence of the new crises

From the view point of not emerging of new financial crises or avoiding deepening of the crisis that may arise, the actions to be able to take in the foreign currency market can be discussed under the following headings (Birinci,1998).

- Taxing the transactions (Tobin Tax)
- Fixing the exchange rates or determining the exchange rate limits
- Application of multiple exchange rates

- Increasing the international banking audit, impeding the capital escape
- Trading halts applications (closing the transactions markets in the crisis environment),
- Establishing the international alarming system
- Increasing IMF quotas
- IMF warranted borrowing easiness
- Organizing the financial movements in the framework of a process similar to GATT
- Target zone system (via international cooperation, preventing the unrealistic exchange rate variations).

The other suggestions are (Eğilmez, 1999: 41):

- Transforming Interim Committee (Interim Committee of The IMF) into the executive council
- Bounding the international system to the rules that ate in international validity
- Transforming G-7 into a decision body in the form of G-15, including the developing countries (J.Sachs, 1999)
- Rescuing IMF from the press of USA Treasure, restoring an independent structure (J.Sachs,1999)
- Completing the financial sector reports in all countries
- For the struggle with corruption and improved and transparent public administration, making worldwide attempts
- Establishing an international debt panel, enabling the various countries to perform their debt reliefs through this panel

In reducing the negative effects of capital flows, the alternative policy applications are putt in order as follows.

- Sterilization of capital flows
- Application of more flexible exchange rate
- Capital controls
- Tight fiscal policies
- Tightening the monetary policy in response to capital escape
- Fortifying the banking system

It is known that the short-term capital movements cause crises. To prevent these crises, various policies are applied. One of the major policies is capital control. The most discussed policy was Tobin tax.

In reducing the effects of short-term capital movements, can Tobin tax be a solution?

Global capital movements are examined as indirect investments, short termed monetary capital, central and fiscal funds, speculative fund flows, and money laundering.

Foreign capital investments are collected in two groups. One of them is the portfolio investment, in other words, hot money; the second is capital to be brought in the way that it will increase the production capacity of country. Portfolio investments are short-term. These kind of investments very rapidly leave the country at the moment of a crisis and become deeper the dimension of crisis (Acar, 2003).

When the controls on the capital movements are removed, there is a movement of capital inflow toward the developing countries. The reason for this, with the rise of interest rates in developing countries, is that they rise above the average of the world. Since this also means a profitable investment for the foreign investors, a capital flow occurs toward the developing countries. The relationship between the short-term capital movements and exchange rate occupies an important place in shaping of financial crises. In the conditions of floating or free exchange rate or in the conditions of fixed exchange rates exposed to frequent changes, it is possible to avoid the risk of foreign exchange. If one can avoid the risks of foreign exchange, the short-term capital movements cannot occur. Since the risks of foreign exchanges are consciously undertaken, when short-term capital movements occur, these provide the stability and become an element of instability (Kındleberger, 1970).

Capital flows becoming free, under the press of the profit rate to fall, causes the capital to leave its country of origin with higher return. If it reaches a developing countries, whose financial markets are vulnerable, it becomes source of a great fiscal instability, accelerating the speculative movements, concluding with crisis. Interest arbitrage includes very short-term capital movements and portfolio investments, because, theoretically, the differences between international interest rates domestic interest rates largely cause the short-term capital movements (Işık-Duman-Korkmaz, 2004: 59).).

There are three main features of speculations. First is that there is an descent of a rise and that speculative rises conclude with a collapse. The second one is that there are losers in response to the winner and in a general sum, is that the case that no income can be created via speculation. The last is, in the real production sectors, when the profitability rate of capital decreases, that the speculations gain intensity and that demands for fund is created.

Black money, very generally, is the value of every kind of property, expressed income and money obtained by offending. The identity and citizenship of the funds that enter and leave the countries in the form of fluid funds is uncertain. Liberalization of capital movements accelerated the formation of black money. Some part of unrecorded economy is related to the common but local practices of the recorded firms such as tax evasion, not paying for social security premium, and understating the number of wage of workers. Some part of it consists of the crimes such as arms smuggling, drug trafficking, terror financing, and winning international tender by corruption, in which the people of a number of globalizing country are included. The size of its dimensions made a current issue that the black money sourced funds must absolutely find a way to gain favor and to be cleaned and the important role in the financial crisis especially experienced in the developing countries (Kazan, 2005).

In 1972, James Tobin, in his book, in order to reduce the negative effects of short-term capital movements, gave a suggestion. This suggestion is that a single type of transformation tax that will be collected in the spot markets, where a foreign currency is converted to another one, will prevent the circulation of short termed capital movements. As far as James Tobin disturbed that international transaction tax, suggested by himself turned into opposition to globalization, this precaution placed gave priority to the suggestions about impeding the short-term capital movements (Akdiş,2004). Tobin suggests that the tax offered by him should be applied to all financial instruments. According to Tobin, this tax should be applied in case that a currency unit purchases the good, service, and real estate in the region, where another currency unit is valid, This offer by Tobin identifying with the words of "throw sand in the wheels" includes to impose tax to the short termed and high summed capital movements that disproportionally actualize in the global exchange rate markets (Westerhoff, 2003: 2). James Tobin suggested to apply a tax that includes foreign currency exchange and that will affect all international foreign currency transactions. The tax of interest will come into play in both buying and selling whatever the aim of transactions is. In the beginning, it was considered that this tax should be applied in only current market, but the multiplicity of dodges in the current market revealed that the tax should encompass all markets (Ciritçi, 2004: 57).

It is considered that Tobin tax is collected through the transactions of foreign currency exchange in a single and very low rate according to ad valorem base. Tobin himself suggested these can be in the rates of such as 0,2% , 0,5%, and 1%. Tobin, suggesting that the financial crisis rising in Asia demonstrated how volatile foreign currency exchange system is, expressed that a global tax to be able to levy through foreign currency exchange is one of the probabilities to solve the problem of excessive volatility (Akdiş,2004). Provided that the scope of Tobin tax can be extended in such a way that it will include at least the markets of future options and swap, it will always be possibilities to avoid this kind of taxes. When compared to the development of spot markets, the derivative markets, in the recent years, show a rapid development all over the world. This situation forms a reason for including the derivatives transactions in the scope of tax. When the tax is imposed, with the thought that the new financial instruments can be invented, which are not included in the scope of tax, it will be necessary to extend the scope of tax in such a way that it will include the sorts of security and derivatives market instrument to be able to emerge further (Yılmaz, 2002: 9). In the application of Tobin tax, the transactions of foreign currency exchange of national states, central banks, and international official organizations and very small sized transactions are exempted from Tobin tax (Patterson and Galliano, 1998: 29). In addition, the regions of monetary union are in the scope of exemption.

In Table 1, a summary of capital control applied in the world is presented.

Table 1. World applications toward controlling the capital movements in the selected countries

Countries	Year	Reason	Control mechanism of capital movement	Results
Europe and Latin America	929	1929 Economic depression	Foreign currency controlled	Successful
ABD	1960	Depending ohm the tendencies, in the direction of liberalization, that capital outflows are experienced	Levying the tax on the capital outflows – tax on equalizing the real interest rate	Partially successful (It has no remarkable effect in reducing speculation)
Israel	1996	Limitation of capital inflows to the country	Levying the tax on the capital inflows	Partially successful (It has no remarkable effect in reducing speculation)
Malaysia	1998	1997 Asia Crisis	The controls made on the outflows of capital - limitation of Malaysian citizens to invest capital abroad and stopping the inlet of foreign investments for 12 months	Successful
Chile	1978-1982 1991-1998	Banking Crises	Controls on capital inflows - imposing the non-profit reserve deposit obligation ohm the portfolio investments	Successful
Brazil	1998	1997 Asia Crisis	Control of capital outflows – transaction tax - imposing General Transfer tax ohm banking transfers in the rate of 0.25%	Unsuccessful

Source: Fatih Mehmet Ocal, 2012

According to the table, the applications of Malaysia, Chile, Latin America countries, and Europe became successful, Brazil successful, and USA partially successful.

In an alternative way to Tobin tax, some polices are suggested. These are:

- Tax on Foreign Securities
- Tax on the Capital Inflows and Outflows
- Tax on the Capital Gains

There are some points that are dominant in the application of Tobin tax. These are (Patterson and Galliano, 1998: 29):

1. As the number of foreign currency exchange transactions increases, the effective tax rate increases .
2. Tobin tax will not make all speculative transactions non-profit and impossible and will only raise the rate of risk.

The possible benefits of Tobin tax (Halifax, 2003)

- With the decrease of transaction volume in the foreign exchange markets, the volatility of foreign currency will fall and stability will mobilize the trade of goods and services.
- This tax will provide financial support in the runs between economies. The possible damages of tax are put in order as follows:
- Application of such a tax serves as an instrument of only short-term monetary policy (Span, 1996: 8)
- To be able to apply the tax, it will be necessary to make an agreement with each financial center in the world; otherwise, the foreign currency markets will go toward the tax –free transactions and the countries, tax heaven (Raffer, 1998: 534). That such a tax is simultaneously executed by all countries is not applicable from the technical and political point of view (Edwards, 1999: 2).
- Applying such a tax will bring a bureaucratic charge to the market, in which $1 – 1.5 million is revolved.
- Another issue is that imposing a tax on the foreign currency transaction will be able to switch the direction of international capital to the derivatives markets and it will go toward the commercial papers and acceptance of banker (Spahn, 1996:2).
- If the exchange rate is face to face with the speculative stocks, speculators, considering the tax charge on the transactions they carried out, will move and this will be able to increase the volatility rather than reducing.
- In the literature, there are some views supporting and opposing Tobin tax. Table 2 includes the views on Tobin tax.

Table 2. The views on Tobin Tax

For	Against
It brings stability to the international financial markets, preventing the speculative monetary movements	It serves as a short-term monetary policy instrument, that it is not an effective instrument in eliminating the economic instability
with the struggle with instabilities the speculative capital led to, its fortifying the internal resources of the country	it negatively affects the development of financial markets in the developing countries
By reducing the rate of Tobin tax according to the maturity, it encourages longer termed foreign capital	When the short-term capital leaves the country, it increases the budgetary deficits
Obtaining tax income and using this income for regulating international markets	Since Tobin tax, depending on the technical and political differences, cannot be simultaneously applied by all countries, the foreign capital goes toward the tax-free transactions and the countries that ate tax heaven
With preventing the speculative capital movements, providing the stability in exchange rates and interest rates	Since Tobin tax does not satisfy the expectations of governments in case that the lower tax base forms, the fact that the tax incomes below that hoped
That IMF and World Bank provide the resource for the international stability programs and solution of social problems of the world	The thought that the taxes can be applied toward capital movements will deviate the financial markets; direct the investors; and keep the financiers out of the economy and sector or shift them to the regions exempted from tax
Together with the increase of short-term capital transactions, making the foreign investments in the long period, and depending on this, stimulation of the real sector	That makes the variable tax rates, tax accountabilities, and responsibilities on the tax administration complicated and that such a tax imposed ohm the capital movements reduces the effectiveness in the market
Subjecting the transactions of multinational companies that have avoided taxation to international tax	In case that with tax, the short-term capital movements decrease, constriction of trading volume; and with increase in the volatility, that exchange rate cannot realize the commercial gains
With Tobin tax, that the governments are rid of the press on the country currency and that they can more easily the economic policies	That the size of additional charge to be put on the transactions is not well calculated and depending ohm its high taxing, its raising the transaction costs and reducing the trading volume; and its negatively affecting the long termed investment

Source: Fatih Mehmet Ocal, 2012

Conclusion

Integration of financial markets and the developing countries have been caught off-guard which has made the economies vulnerable. Especially, using the short-term capital movement with the speculative purposes increases this vulnerability and creases an effect disturbing the financial stability. To reduce the vulnerabilities of economies and make them less sensitive to the capital movement, a lot of precautions were emphasized. The major one among these precautions is capital controls, while in the capital controls; the most emphasized and discussed was Tobin tax.

James Tobin suggests an ad valorem tax in order for the capital to stay for long term in the county once it enters it. This tax expresses a lower rate such as 0.2%, 0.5%, and 1%. This tax of lower rate, when considering the size of trading volume, corresponds to a large amount in the way of not being able to ignore.

Malaysia and Chile, with the limitation they bought to the inflows and outflows of capital, managed to provide the financial stability. The tax does not affect the long termed capital outflows and only aims to constrain the short termed capital inflows. The major criticism brought to Tobin tax is bureaucratic charge and international capital that will go toward derivatives markets. The economic crises experienced by the developing countries showed that that the economies included in the financial markets without making the necessary preparations makes an effect which disturbs the stability. What should be done is include them in the financial system without disturbing the economic stability. The way of realizing this is that the financial markets become deeper and more developed. If it was integrated to the system without providing this depth and development, the vulnerability of economies becomes unavoidable and it is moved to search for ways to reduce vulnerability. The capital controls are considered as the best way to conduct the search. The capital controls stand out as an important instrument in reducing the effects of capital movements.

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