Joseph Yam: Speech at the Asian Development Bank Annual Meeting

Speech by Mr Joseph Yam, Chief Executive of the Hong Kong Monetary Authority, at the 33rd Asian Development Bank Annual Meeting, held in Chiang Mai, on 6-8 May 2000.

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Mr President, I would like first to express my gratitude to the people and Government of Thailand for their generous hospitality in hosting this year's Annual Meeting of the Asian Development Bank. I would also like to thank the Bank's management and staff for the excellent arrangements for this meeting.

Mr President, notwithstanding the devastating Asian financial turmoil of 1997-98, the development record of Asia in recent times has been impressive. The Asian Development Bank has played an important role in making this impressive record possible and I must, in this first Annual Meeting of the Bank in the new millennium, record my appreciation of the good work that the Bank, since its establishment, has done for our region.

But like everything else, and everybody else, the Bank could have done even better for Asia had it been able to foresee, and promote policies capable of pre-empting the financial crisis which has brought so much suffering and disruption to the region. In our enjoyment of the Asian miracle, we, whether within or outside the region, were all oblivious of the risks associated with the explosion of international finance that we have recently been experiencing. But as markets attained a global dimension, encouraged by financial liberalisation and the advance of information technology, they became far less tolerant of weaknesses than before, and the markets responded to weaknesses with harsh punishments, which many considered grossly unfair.

But this is the reality that we face. And if we are to continue to benefit from the greatly enhanced efficiency of global financial markets in international financial intermediation - a process that has contributed so much to development - we have to get on with the necessary reforms. These include the domestic structural reforms to the financial and corporate sectors, to make sure that we can manage the risks and cope with the volatility that are part of that efficiency. And, to the extent that consensus can be reached, they also include measures to strengthen the international financial architecture.

Thus, with some encouragement from the Bank and from others, and more importantly, urged on by the brute forces of the market, significant progress has been made in the domestic structural reforms of individual economies in the region. I applaud the progress and the achievements; and I sympathise with the pain and suffering which they have entailed. With the economic recovery of the region now well under way and international funds flowing back into the region, I would also urge a continued commitment to structural reforms and caution against complacency. It must be recognised that structural reforms, and specifically financial sector reform, is of crucial importance if this recovery is to be turned into sustainable economic growth. A bank with the mandate to promote development in Asia must surely have a role to play in all this and I look forward to greater involvement of the Bank, in whatever capacity, in maintaining the momentum of structural reforms in Asia.

Mr President, the efficiency of financial markets in the region in performing the important function of financial intermediation has been found lacking. There has been notably little disagreement about the desirability of developing domestic and regional bond markets. But there has also been little progress. And there has been no lack of explanation of why this is the case. The often quoted impediments include the lack of clearing and settlement infrastructure, the absence of a broad institutional investor base, the lack of a benchmark yield curve, low liquidity, and so on. While these impediments are recognised and are being tackled earnestly by national authorities, there is one problem that has attracted relatively little attention so far. The problem relates to the generally low credit ratings of the Asian issuers, including the sovereigns, granted by the international rating agencies.

I do not wish to provoke a debate on the objectivity and reliability of the ratings and the rating process of the international rating agencies. The reality is that many Asian governments and corporations receive credit ratings that are lower than the minimum thresholds acceptable to institutional investors, including the managers of official reserves. There is certainly merit in strengthening the dialogue between the Asian issuers and the international credit agencies to facilitate a better understanding of the Asian situation by the rating agencies and improve the transparency and accountability of the rating process. There is also a case for considering whether it is advisable or viable to establish national or regional credit rating agencies, with or without support from the authorities. On top of these, I think there is a need to consider the introduction of market-based mechanisms for credit enhancement or guarantees.

In Asia, I am aware of problems encountered by private sector initiatives in this field. It has proved difficult objectively to assess and manage the risks involved in such operations. Indeed, one feature of the recent explosion of international finance is market volatility that has been much higher than had been thought possible in the light of historical experience. But I think we have learnt from the recent years of financial turmoil and I hope we are now in a better position to identify and therefore properly price the risks involved in the provision of credit enhancements or guarantees. What, for example, the Bank and the Miyazawa Plan have achieved in the provision of credit guarantees to several sovereign bond issues after the outbreak of the financial crisis could also be achieved and expanded through market based arrangements.

Credit enhancement is quite common in the developed markets. In the US, the credit guarantee companies were insuring around US$ 278.5 billion of debt securities at the end of 1998. The availability and use of credit enhancement facilities have become a basic ingredient of mature bond markets. It will be useful to examine how this could be promoted in the region. This promises to give a much-needed boost to the development of the bond market in the region.

Mr President, let me end by expressing confidence that the Bank, under your leadership, will be able to play a more pivotal role in the development of Asia as it steps into a new era in which technology presents an abundance of opportunities as well as risks.