

Tanya Sirivedhin: New challenges for finance and capital markets

Speech by Ms Tanya Sirivedhin, Deputy Governor of the Bank of Thailand, at the Conference on “Thailand-Finance and Capital Markets”, held in Bangkok, on 28 September 2000.

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Today’s conference is very timely, in view of the increasing role that finance and capital markets are likely to play in the future Thai financial scene.

I have identified several aspects of the challenges of “Finance and Capital Markets” which I would like to share with this audience. I hope that the open discussion of these challenges will be an important input into the work of the Thai authorities, and what we envisage to be the vision for our industry.

I shall frame the challenges in three dimensions:

First, the challenges from rebuilding and strengthening the business and financial industry.

Second, the challenges from the adoption of best international practices.

Third, the challenges from the race to catch up with the new technological frontier of e-commerce and electronic trading.

Rebuilding and strengthening the financial industry

The 1997 economic and financial crisis brought to light many weaknesses in Thailand’s macroeconomic and financial management. In its aftermath, measures were undertaken speedily to shore up the currency and to restore confidence in the viability and sustainability of firms and businesses, both in the financial and non-financial industry. Through the implementation of these measures, there were inevitably many casualties. For example, as many as 56 finance companies were closed down permanently while others, as well as the weak banks, were taken over by the authorities or consolidated. Businesses caught short by the depreciation of the currency or the austere belt tightening environment which lifted interest rates to historically high levels, had to be closed down or consolidated.

It became of utmost urgency to improve confidence, strengthen the operations of financial institutions and enable them to improve and resume their intermediation role. In the view of the Bank of Thailand, the only way to bring about sustained recovery of the economy which was affected by the liquidity crunch situation, and by the concern over counterparty credit risks in the midst of the crisis, was to tackle head-on the issue of non-performing loans.

In June 1998, the Bank of Thailand, in cooperation with five associations, namely, Thai Bankers’ Association, Foreign Banks’ Association, Association of Finance Companies, Board of Trade, and Federation of Thai Industries, set up the Corporate Debt Restructuring Advisory Committee (CDRAC). This was aimed to oversee and facilitate the out-of-court debt restructuring process. Its mandate was to help push ahead complicated debt restructuring cases through a framework of negotiation. The Committee also pushed through many initiatives to eliminate legal and tax obstacles to debt restructuring.

Consequently, NPLs in the financial system have fallen progressively from a peak of 47% of total loans in May 1999, to the present level of about 31% of total loans. The decline is partly the result of debt restructuring, as well as transfers of non-performing loans to Asset Management Companies (AMCs). As at the end of July 2000, restructured debt totalled 281,222 cases with a corresponding credit outstanding of 1.7 trillion baht, while cases in the process of restructuring totalled 22,906 with a corresponding credit outstanding of about 773 billion baht. With cleaner balance sheets, banks are in a better position to start lending.

Now that the situation has stabilized, post-crisis rebuilding and reconstruction in the banking system must be pursued vigorously, both through policy-induced means as well as through individual firms' initiatives. To reduce reliance on bank credit, the capital market must be developed as an alternative channel for funding. This will help rectify an important weakness of the past whereby firms relied excessively on bank borrowing and were not able to access funds directly from the capital market. Among initiatives to promote the capital market which are being pursued by the authorities are the development of the domestic bond market, the corporatization of the Stock Exchange of Thailand (SET) to widen membership and participation, as well as acceleration of the privatization process to increase the supply of new listings on the SET.

Looking ahead, competition facing the financial industry will come not only from the entry of new participants, especially foreign players, but from competition across industries or frontiers such as between banks and securities firms.

Operational boundaries are becoming more and more blurred with the much debated argument of a universal versus a segregated banking system. Yet the future landscape of the industry in regard to business operations of financial institutions is increasingly more challenging as technological competition encroaches on all fronts. Electronic trading platforms for bonds, accessible to both banks and securities houses, will gradually erode the role of these intermediaries. Customers can easily access a trading platform, searching for the best quotation to serve their needs and investment horizons. These electronic trading platforms can easily service the traditional customers of banks and securities firms, such as pension funds, provident funds, mutual funds and insurance, without the need for an intermediary network of dealers. Traditional dealers, accustomed to the OTC market trading environment and relationship with their customers will need to prepare themselves for a new market niche for the future. These could include upgrading their research capabilities to provide better research materials for their customers, enhancing efficiency of operation, so as not to be marginalized in the new competitive environment.

No doubt processing simple loan applications and bank lending will remain the bread and butter of the financial industry for some time, but competition will inevitably be stronger with new entries and market participants.

The challenge of adoption of international practices

When a country plunges into a serious crisis, which I may say in the case of Thailand was a crisis of both macroeconomic imbalance and of confidence, drastic measures have to be imposed on all fronts. As such we found ourselves pursuing austere macroeconomic policy, which worked to curtail excessive spending and restrain aggregate demand, thereby improving Thailand's external accounts and stemming capital outflows. At the same time, we had to adopt stricter prudential standards to raise confidence in our financial institutions. Banks inevitably had to scramble to raise capital in order to meet the provisioning requirements under our new and stricter definition of "non-performing loan".

In addition to the adoption of international best practice with regard to asset classification and provisioning, other banking practices had to be upgraded. For example the industry has had to get used to a new way of doing business, pursuing good corporate governance, improved disclosure, stronger accountability and better risk management and control. These are indeed significant changes from the traditional way business had been conducted in the past, and in turn will need commitment of management and staff, inputs and resources to bring the industry to full compliance with international best practices, not to mention a new supervision framework for the authorities.

The new financial institution law, pending consideration by Parliament, will provide the BOT with a clear mandate and accountability to regulate and supervise financial institutions under a new framework, including such procedures as prompt corrective action, and reduced scope for use of judgment, among other things.

On our part, the central bank has also gone through a process of self-examination. We have mapped out a clear strategic direction to ensure that our operational framework focuses on the primary responsibility of achieving financial and monetary stability. Among the major changes being proposed

in the new Bank of Thailand Act is the adoption of inflation targeting as a framework for monetary policy. This is aimed to provide a clear and transparent rule of operation and signaling to market participants. The proposed amendment of the Bank of Thailand Act clearly states that the overriding objective of the central bank is price stability. To implement this, a Monetary Policy Committee has been set up, the results of whose deliberation are to be disclosed regularly to the public, and an Inflation Report is to be published quarterly. As for our supervision function, we are moving towards a risk-focused supervision and improved disclosure and accountability system. The formal policy framework is to be set by the Financial Institution Policy Committee which similarly has members from outside the BOT.

May I add that to expedite the promotion of transparency, we have set up these two committees even before the new law has come into effect. Thus highly respected and well qualified outside persons now have a say in the deliberations on both monetary policy and financial institution policy.

The technological challenge

The 1997 crisis set back economic and financial development in Thailand by many years. These have to be made up through speedier reforms and a catching up process. In addition financial market participants as well as regulators are facing the global challenge of the new economy and technological revolution.

The new technological revolution is pushing for change everywhere in the world, and with no concern for those in need of time to heal the wounds inflicted by crisis. It has become an inevitable development which needs to be embraced with the right attitude, mindset and understanding.

The new economy in itself poses challenges, not exclusively to financial service providers, but to regulators, business operators and the financial industry as a whole. The challenge, on this last aspect, is particularly crucial to the government sector; for they need to make sure that the legal, regulatory and supervisory framework are there to create the right competitive environment and operating conditions. This is to ensure that when their own private operators are ready for the technological challenges of E-banking, internet-broking and the electronic trading platform, then the appropriate legal and regulatory framework is there, rather than becoming an obstacle to development - by which time we may no longer be able to catch up with major global players.

In the world of E-commerce and trading, banks have become important intermediaries as the operator of the payments system, to facilitate the payment for the goods and services which are being traded on-line. As regulator of the commercial banking business, the Bank of Thailand is working in earnest to support the development of the country's payment system, by both the public and private sectors. This is to ensure that the country's overall payment system is fully integrated and contributes positively to the overall efficiency of trade and commerce within and outside the country. This in turn will enhance the country's capacity to face competition and challenges in the international financial and investment environment, at the regional and global levels. Nevertheless, while information technology proceeds at the speed of light, the corresponding legislative reforms take time. The Bank of Thailand, along with other government agencies, is working hard to push forward for the enactment of crucial legislations such as the Electronic Transaction Act, Electronic Digital Law, Electronic Fund Transfer, to name but a few.

Technological revolution in the banking and financial world, such as the advent of E-money, have had an impact on fundamental central banking concerns, particularly on the definition of "money", the transmission mechanism of monetary policy and the traditional intermediation function of banks and deposit taking institutions. These, in turn, will likely make the conduct of monetary policy more difficult and challenging. Monetary authorities will need to stay on top of these developments.

Finally, let me conclude by hoping that I have left you with some food for thought for your further deliberation and discussion. May I also take this opportunity to thank the organizers of the Conference on Finance and Capital Markets for inviting me here today.