Prasarn Trairatvorakul: Financing the Greater Mekong Subregion

Keynote address by Dr Prasarn Trairatvorakul, Governor of the Bank of Thailand, at the Euromoney Greater Mekong Subregion Investment Forum, Bangkok, 20 June 2012.

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Excellencies, Honorable speakers

Distinguished guests; Ladies and Gentlemen

It is an honour to be a part of the Greater Mekong Investment Forum and a great pleasure to commemorate the 20-year anniversary of the Asian Development Bank Greater Mekong Subregion (GMS) Economic Cooperation Program. I would like to thank the Euromoney for inviting me to speak today.

The shift in the world's center of gravity towards "rising Asia" has been widely recognized and well documented. But within the Asian region lies the Mekong Subregion which the ADB has been financing and providing technical assistance for more than two decades. Today this region is getting much of the world's interest and attention. ***The rich human and natural resource endowments as well as the complementary diversity of the Greater Mekong Subregion have made it the new frontier of South East Asian economic growth.*** The GMS stands among the world's fastest growing areas, registering a 10-year-average growth of around 8%, followed by the BRIC nations at 6.7% and Sub-Sahara Africa at 5.5%.

The global attention and interest on this region means prospects for increasing trade and investment. Financial services as we all know are derived demand from the needs of the real economy for trade and investment opportunities. Though not taking a driving seat, ***a financial system that is safe and sound has an important role to support growth and sustainable development.***

When it comes to finance, three issues come to my mind. First, what should be the strategy for meeting the financing needs of the Subregion. Second, what role should the Thai financial system play as an intermediary and as a member of the GMS. Third, what are the regulatory and institutional challenges to ensure financial stability and sustainable development.

On the first issue of financing, we generally observe that trade and direct investment flows are largely influenced by proximity and endowment. ***Finance, on the other hand, knows no boundary.***

Given the broad-based financing needs of the GMS which range from large scale project finance to commercial banking for SME, there is a role for all types of institutions: local, regional and global.

(1) ***For local financial institutions, their knowledge and understanding should give them a comparative advantage to support the traditional sectors that are the mainstay of the region, namely the agricultural sector, household and small entrepreneurs. In this way, they have a predominant role in promoting financial inclusion.*** Non-bank institutions or innovative financial services such as microfinance, mobile and e-banking and remittance services help promote financial access for households and enterprises.

(2) ***For larger corporate or infrastructural projects that local or regional banks might not have the financial capacity or know how, there is a role for global institutions*** to lead finance or underwrite. But global institutions would need local guides to venture into new markets. Here there is a role for local or regional banks to partner with global banks.

(3) ***As to who should be borrowing, given the public goods nature of the long term infrastructural projects, the government should take the lead.*** Options for financing include direct government borrowing, concessional borrowing from overseas development assistance, or through Public Private Partnership (PPP).

(4) ***Beyond banking, developments in the capital market and regional cooperation initiatives provide channel to intermediate cross border savings to finance infrastructure investments.*** These include the ASEAN Infrastructure Fund (AIF), the Credit Guarantee Investment Facility (CGIF), and Asian Bond Market Initiative (ABMI).

Going forward, the combination of the above arrangements should provide a division of task that is healthy and balanced for the region.

Secondly, on the role of Thai financial intermediaries, I see the following prospects for the Subregion. ***In addition to our strength in core banking business, the Thai banking sector has been partnering with foreign entities to serve the broad-based demands of the economy. Thus, we can play a meaningful role in bridging between the global financial players and the smaller local intermediaries. We can also contribute in terms of expertise and experiences.***

- ***So what is Thailand's value proposition? Thai banks can play a role and compete in the business of financing small and medium enterprises.*** And with the natural trade links and the people-to-people relations, there is a role for Thai banks in the payments and remittance services. These areas may not be commercially viable for global banks if the scale of the transaction is deemed too small. But for Thailand, such basic services can help support the robust growth of cross border trade and investments which are important for rural development and income distribution.
- With the fundamental trend where Thai businesses start to diversify investment and production base to neighboring GMS countries, it is natural for Thai financial institutions to follow their clients. ***Thai banks therefore have an important role in partnering Thai and GMS corporates. Areas such as project evaluation, business-set up, cross-border financial transaction are areas where the local know how matter and where Thai banks can meaningfully contribute.*** Through the vertical integration of these corporate finance services, Thai financial institutions naturally become an intermediary between Thai business and our GMS counterpart. As clients organize themselves around a regional supply chain, Thai banks become a natural partner to bring GMS business and investment to Thailand. Thai banks and their GMS correspondent banks or joint venture partners have a niche market advantage. They have close business links, geographical advantage, and access to funding in local currencies which are the natural means of payment for intraregional trade.
- Thailand is therefore poised to assume the role of a ***connector – by acting as a link or point of reference for the entry of global banks into the subregion.*** This is underpinned by our established financial platform, familiarity with the local business practices, as well as close cultural ties among our people.
- ***Of equal importance is our own inherent understanding of the challenges of developments faced by GMS, through our own experience.*** This is particularly important in two aspects.
- ***First, Thai financial institutions are still focused on core financial intermediary functions*** such as payments services, deposit, and loans which serve the basic needs of the real sector. Thai banks are inclined to serve the needs of the real economy rather than in speculative types of businesses such as proprietary trading. For these reasons, Thai banks are also less complex, with good risk management

and strong capital base. Regulators in Thailand and GMS neighbours can understand fairly well the business model of our banks and their risk. We believe that given the lesson of the current global crisis, this type of bank model makes good sense for home and host regulators.

- Secondly, both regulator and the banks in Thailand could well remember the bitter experience of our own economic and financial crisis in 1997. ***We understand that financial liberalization needs to be properly sequenced. We also understand that financial development must be underpinned by a solid foundation suitable for each country's economic, social, and political context.*** The speed of liberalization and change must not be too fast that it overtakes the fundamental preconditions such as strong financial laws, the ability to regulate and manage risk and the financial literacy of people. Failure to satisfy these prerequisites risks creating imbalances in the macroeconomy that cause financial instability. With this awareness and the experience still fresh in our mind, I believe we are a natural and understanding partner in the development process. Our banks can relate to and respect the local context in the GMS countries. They can adapt to it as well as share the experiences. Joint ventures, correspondent banking, as well as regulatory and supervisory cooperation are ideal for capacity building. Indeed, close proximity as well as common language and cultural heritage also help relay the experiences.

Lastly, the task of financial development would not be complete without the supporting infrastructures, institutional set up, and risk management system. This entails but is not limited to

(1) ***the adoption of a robust regulatory framework*** to ensure prudent conducts of financial intermediaries that foster an open and competitive regime;

(2) ***appropriate monitoring and policy tools*** to detect occasional imbalances, flag early warning signals and encourage quick remedial actions;

(3) ***talent training and development*** to manage risks and drive continuous advancement of the financial sector and;

(4) ***good governance, predictability and ease of doing business.*** Such discipline would bring about credibility which is crucial to maintaining the attraction of the region and continued foreign investment.

So far, much progress has been made and vast opportunities can be seen going forward. We are well aware that greater benefits are achieved from synergies and coordination rather than autonomous actions. Further efforts to ***Connect***, to collectively enhance **Competitiveness** and to promote a sense of ***Community – the 3C's, must be pursued – both in trade and in finance, and within the public as well as the private sector.*** Ultimately, strengthening the Greater Mekong Subregion would be our best contribution to reaching the goal of our ASEAN Economic Community.

On this note, let me thank you for your attention and for your interest in our region.