Asian financial cooperation as seen from Europe

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It is a great pleasure for me to attend this conference, jointly organised by Korea University and the BIS. We at the BIS have organised conferences with monetary institutions in the region, including the State Administration of Foreign Exchange in Beijing and the Bank of Thailand in Bangkok, but this is the first with an academic institution in the region. We take this opportunity to salute Korea University on its 100th anniversary and to wish it well in its next century. As Seoul aspires to become a hub for Northeast Asia, Korea's world-class centres of learning will come into their own.

We meet in this splendid academic environment to discuss a practical and topical subject. The work to be reported and commented on here is certainly of great relevance to a matter that is enjoying high priority on the agenda of Asian policymakers, namely promoting the development of Asian bond markets.

In fact, I am convinced that steps to promote the Asian bond market have the potential to make a contribution to monetary and financial cooperation in Asia that goes beyond simply deepening and enhancing the efficiency of today's bond markets. Let me explain what I have in mind by looking at Asian monetary cooperation through the European rear-view mirror. In doing so, I will first make some broad-brush comparisons between Asian and European developments and then present some observations on the forces that, in my mind, have driven the process of cooperation in Europe - leaving it to you to decide whether a similar development could be expected in Asia.

At the risk of oversimplifying, there are at least two developments that are prompting closer monetary cooperation in Asia even as they did in Europe. The first is a marked increase in trade integration across the region, accompanied by the emergence of poles of economic growth independent of US demand and by a growing awareness of vulnerability to exchange rate changes.

In Europe, this process was partly the result and partly the cause of closer monetary cooperation. And I am proud to say that the BIS, in offering technical and meeting-related support, played an important role in this process. Without going into detail, let me illustrate this with a couple of examples. Between 1950 and 1958 the European Payments Union used the BIS as an agent to permit the multilateralisation of bilateral surpluses and deficits in Europe, thus preparing the ground for a return to current account convertibility. In the Treaty of Rome of 1958 the European Community established the Monetary Committee, composed of very senior central bank and finance ministry officials. And in 1964 the European central banks set up the Committee of Governors as their central forum for cooperation. This Committee met for 30 years at the BIS - until a new European institution was established in Frankfurt.

In Asia the response to growing regional integration broadly paralleled the European development. Regional central bank forums were launched, such as SEANZA (in 1957) and SEACEN (formally in 1982), to promote joint training and research. EMEAP started in 1991, operating first at Deputy Governor and later at Governor level, and soon established working groups in three financial areas of particular concern to central banks. In fact, these groups complemented those which had been in existence at the BIS for many years.

The second common trend in the development of monetary cooperation in Asia and Europe was the impact of crises on the building of institutional arrangements. In Europe, the shock of the collapse of the Bretton Woods system and the beginning of generalised floating prompted the creation of the so-called narrow margins arrangement, better known as the "snake", supported by the European Monetary Cooperation Fund (EMCF), which settled intervention balances and provided short-term balance of payments support. Incidentally, this Fund existed more on paper - all operations were performed by the BIS acting as agent. Still, the record of these early efforts at monetary and exchange rate stability was pretty chequered, as inflation differentials necessitated parity changes and/or forced countries to opt out of the system.

The shock of the foreign exchange and banking crisis in Asia in 1997-98 also initiated steps towards building firmer institutional structures - though not necessarily of the kind set up in Europe. The main strategy for building defences against currency crises was to increase the availability of reserves, either through swap lines as agreed by ASEAN+3 under the Chiang Mai Initiative, or simply by bolstering reserves as a kind of self-insurance. A different and, in its multilateral character, potentially far-reaching institutional measure was EMEAP's launching last June of the Asian Bond Fund (ABF) in dollar-denominated instruments, aimed at promoting the development of a regional bond market. It was recognised that a dollar-denominated fund was the art of the possible rather than the desideratum. Accordingly, active discussions are now under way to add a second ABF in domestic currency. An extremely significant and multipronged approach to improving the underlying financial structure is being pursued in parallel by ASEAN+3.

These developments in monetary cooperation pertain mainly to the past, with Asia lagging behind Europe, where such cooperation led in 1999 to the creation of a single currency and a common central bank. Naturally, this gives rise to the speculative question of whether developments in Asia will take the same turn, that is, follow the European path. Since we at the BIS do not speculate, I can neatly sidestep this question. However, having been closely involved for many years in the process of European monetary cooperation, I can highlight some of the forces that were instrumental in reaching the goal of monetary unification. Then I shall leave it to you to infer what this could mean for future monetary cooperation in Asia.

Let me start with two more principal observations. The first is that the move towards monetary union in Europe was foremost a political process. Without the political will and impetus, monetary and financial integration at today's level could not have happened.

Having said this, my second principal observation is that the political objective of monetary union would also not have been achieved without the active part played by the financial authorities and, in particular, the central banks. Just to remind you, the breakthrough in moving to monetary union was based on a blueprint of how to realise monetary union (the Delors Report of 1989) presented by a group of central bank Governors.

But, in addition to these points, I would identify at least three lessons to be drawn from the process of monetary cooperation in Europe.

First, financing arrangements such as short-term swaps or medium-term balance of payments loans (as granted by the EMCF and the European Community during the first phase of the exchange rate mechanism) have frequently been cited as an important prerequisite for the success of the exchange rate arrangements. I doubt that their contribution in terms of providing financial resources was really decisive, but I recognise that these mechanisms were sometimes of enormous psychological and tactical importance for coming to an agreement in the negotiations.

Second, institutional aspects matter. European experience, however, suggests that big institutional structures are not necessary for success - at least not until the moment that responsibility for policy is transferred to a new, common institution. In fact, the process of European central bank cooperation relied for decades on a very small permanent secretariat, working independently under the roof of the BIS.

Third, there is nothing better than an operational framework to promote and focus monetary cooperation. Such a framework could be a swap arrangement requiring accounting and settlement services, or it could be an ABF or some form of exchange rate mechanism. What matters is that any such arrangement makes it necessary to meet, to exchange views and to take decisions in common. This in turn builds knowledge and mutual trust, which provide the basis for getting through difficult moments in more ambitious cooperative undertakings.

Let me conclude with these observations and, as I said earlier, I leave it to you to judge to what extent they are relevant for the process of Asian monetary cooperation. In one respect, however, I am certain the discussions held here between researchers and policymakers form part of the grand tradition of promoting monetary cooperation. On that note, I wish you all a challenging and fruitful exchange of views at this conference.