

Bandid Nijathaworn: Regional financial cooperation - some thoughts on the way forward

Speech by Mr Bandid Nijathaworn, Deputy Governor of the Bank of Thailand, at the APEC Finance and Development Program Annual Forum, Sanya, China, 28 November 2004.

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Thank you

Mr Chairman,

I would like to begin by thanking the Ministry of Finance of the People's Republic of China and the AFDP Secretariat for inviting me to speak this afternoon in Sanya. It is a pleasure and an honour to be here, especially in the presence of so many distinguished experts and policy makers in the region.

Today, I have been asked to speak on regional financial cooperation. This is a subject we all know well and one that many of us spent a lot of time working on in the past years. Given the limitation of time, I would like to focus my talk today by making just two points.

The first is to highlight some of the key achievements that have been made in regional financial cooperation. Next, I would like to share with you some of my thoughts on the way forward, especially on the measures that can be taken to further strengthen the process of financial cooperation in the region.

First, on the achievements

I think there is no doubt that a lot of progress has been made in regional financial cooperation in the past years. This progress has been driven by a combination of factors, but the most important has been the Asian financial crisis itself, which prompted policy makers in the region to recognize the potential benefits of financial cooperation as a mechanism that can allow the region to prevent or to better manage the risks of financial crisis.

Since the 1997-98 crisis, regional financial cooperation has been strengthened in three main ways:

The first is the strengthening of liquidity arrangements, the second is the introduction of regular policy dialogue and surveillance, and the third is the coordination of efforts to develop the region's bond market.

So far, progress which has been made includes an expanding network of Bilateral Swap Agreements between ASEAN and Plus Three countries under the Chiang Mai Initiatives to provide short-term liquidity. There is also the Formal and Informal ASEAN+3 Finance and Central Banks Meetings to exchange information and discuss policy issues, as well as the discussion under the APEC platform. Also, new developments from the Asian Bond Market Initiative and the APEC Forum have also been launched to develop the region's bond market.

My point is that these achievements are important and their realization would not have been possible without the awareness and the determination of the authorities concerned to make them happen. But notwithstanding the progress made, more can definitely be done to bring regional financial cooperation to a level that is on par with the region's economic and financial potentials. This is to say that although the economies of East Asia have recovered and are on the path of sustained growth, regional financial cooperation needs to continue and should substantially move forward. The rationale for this is clear:

First, financial cooperation will lead to a faster pace and a more comprehensive development of the region's financial markets. Such development is crucial for sustaining the momentum of intra-regional trade and investment, a factor that has been instrumental for the region's recent economic success. Going forward, this momentum of intra regional trade and investment has a potential to become a major source of growth for the region, through the promotion the region's domestic demand.

Second, with the globalized flows of finance and capital, maintaining financial markets stability is a key condition for preserving macroeconomic stability. To achieve this, in addition to the pursuance of sound economic and financial policies, the Asian region also needs to have its own financial arrangement. Such an arrangement will help ensure an orderly and stable financial environment such that any emerging vulnerabilities would not pose serious risks to the region's financial markets and

economies. Important in this context, I believe, is for the region to have its own financing facility that draws on the region's own financial strength and resources. With such a facility, there would be greater confidence amongst policy makers in the region that we do have the capability and the capacity to look after our markets and economies if there were to be a major financial distress.

On the basis of this rationale, it is my view that regional financial cooperation should move progressively forward, with the process being further strengthened and the work becoming more focused, aimed at producing more tangible results.

Let me now spare with you my thoughts on the way forward. On this issue, I should say at the outset that the points I am going to make here are not new, and some of them are probably already familiar to you.

The first is the Chiang Mai Initiative or CMI. CMI was created conceptually as a short-term financing facility to help participating members manage their balance of payments shortfalls at a time of financial distress. Although the economies of East Asia are now much stronger than five years ago, CMI should continue to remain a key pillar of regional financial cooperation. This is because it is important for the region to have its own liquidity arrangement that can be called upon when the need arises.

With the crisis now behind us, we do have time to think on how best to improve the existing facility. And, one way we can approach this is to look for ways we can credibly turn the existing arrangement into a facility that emphasizes a greater level of resource commitment by participating members. This is to say that requesting members should be in a position to count on this facility when the need arises. Looking at the improvement from this angle, I think there are three ways we can reflect upon.

The **first** is to make the size of the arrangement larger and more meaningful with respect to possible needs of members. The **second** is the simplicity of the activation process, especially for the first tranche. This is important for giving assurance to participating members that liquidity will be made available in a timely manner. And the **third** is the objective of turning CMI into a multilateral facility at a later stage. This last feature, if realized, will provide the region with its own financial arrangement that can help expand the region's capability in safeguarding financial stability.

It goes without saying that a move to emphasize greater resource commitment by members will entail substantial strengthening in the current regional surveillance process. This is a development that we all should welcome. Strengthening the surveillance process should in fact be a key prior condition for expanding the CMI because it will help make the CMI process credible while reducing the risk of moral hazard.

CMI is currently under review. I hope some of the points I have touched upon will be further explored. But whatever the outcome of the review may be, I am confident that it will signify another important step forward for regional financial cooperation.

My **second** thought is on the region's bond market. Economists in the region have long made known their views that Asia is a region with surplus savings, but the financial surplus of Asia has not been effectively utilize for the benefits of the economies in Asia. This is clearly a missed opportunity. To bridge this shortcoming, the region's financial markets need to be substantially expanded and developed so that the region's markets can effectively allocate surplus savings within the Asian region. The current focus on regional bond market development is therefore a step in the right direction.

But my point today is that while developing the bond market is important, two additional areas of market developments in tandem with the work on the bond market should also be looked at to ensure a balanced development of financial infrastructure in Asia.

The first is human resource: that is the need to build a steady supply of high quality financial personnel to serve the Asian financial markets.

In the short term, this issue can be partly addressed by promoting a greater role of Asian financial institutions in cross-border transactions or businesses within the Asian market. The expanded role of Asian financial institutions will enhance the experience of Asian financial firms in cross-border transactions and help transfer financial skills and technology among market participants in the region.

For the long term, we should be thinking of establishing a regional finance institute that aims specifically to train and develop financial personnel for the Asian market. To me, this type of initiative looks practical and is economically feasible because Asia's large domestic market will always call for substantial demand for trained financial personnel. Such an institute will also play an important role in

supporting the development of financial markets in Asia, as well as producing the next generation of Asian Financiers.

The second area that should also be considered is the harmonization and streamlining of the existing rules and regulations. This is especially important for cross-border capital movements so that the region's financial resources can flow more smoothly between economies in the region. Streamlining rules and regulations will help reduce unnecessary barriers, and through lower transaction costs, will allow a more efficient allocation of resources. For example, measures to protect domestic markets from outside competition may need to be relaxed. Along the same line, there is room to harmonize taxes on capital market transactions so that tax implications are neutral and do not act as a constraint to efficient resource allocation.

Ladies and Gentlemen,

My last thought for today is on ways we should proceed to expedite the pace of regional financial cooperation. At this juncture, there is no disagreement that we all would like to see more and faster progress on regional financial cooperation. And, to ensure its progress, we have seen policy makers in Asia ready and prepared to take bold and important policy actions.

My view is also the same. I also want to see a faster pace of development rather than a slow one. But one also needs to underscore that, to achieve long term sustainability and continuity, the process of development needs to be market driven rather than policy driven. This is important for ensuring that resources would be allocated efficiently and that the direction of development would be in line with the needs of markets, which reflect private sector's priority and expectations.

At the initial stage of development, as is the case now for the Asian Bond Market, government policies and efforts will be important to spearhead the process of growth and development. But once the momentum takes off, market mechanism should take over to ensure that the pace and focus of development are consistent with market expectations. And, at this level, the role of policy should be to support and facilitate market development by streamlining rules and regulations, by facilitating cross-border trade and investment flows, and by providing the necessary financial infrastructure. This approach will help ensure that the region's financial environment remains conducive to private sector activities and participation.

Let me take the opportunity here to stress that, at this juncture of financial markets development in Asia, I think that support from the authorities is still important and remains a crucial factor. But in order to leverage the impact of government's support and involvement to the fullest, it is important for the authorities to be clear and firm on their commitments to develop the markets. Government involvement should also be focused and concentrate on issues that cannot be tackled by private market participants. Importantly, the authorities should engage the private sector early into the process of market development so that the direction of policy and development is aligned with needs of the private sector.

Most of the issues that I have raised today are not new, but they are the important ones. Again, I will not be surprised if many of you are also having the same thoughts. Such convergence of ideas will be good in helping to advance our interest and work on regional financial cooperation. I am confident that we can move forward more rapidly in the direction that will be most beneficial to our economies, while sharing a common vision of greater prosperity and economic well-being for our region.

Thank you for your attention.