ASEAN Financial Integration towards ASEAN 2025: Call for a well-coordinated supervisory and regulatory framework

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Outline

• ASEAN Community and ASEAN Economic Community
• ASEAN Financial Integration Framework (AFIF) and ASEAN Banking Integration Framework (ABIF)
• Current status of ASEAN Economic and Financial integration
• Future steps: what needs to be done?
  – Strategies embedded in the ASEAN Economic Community Blueprint 2025
ASEAN Community

- ASEAN Political Security Community
- ASEAN Economic Community
- ASEAN Socio-Cultural Community
ASEAN: Big potential for Growth

ASEAN ECONOMY

ASEAN GDP 2007-2014:

- **2007:** US$1.33 trillion
- **2014:** US$2.57 trillion

ASEAN GDP in 2014 almost doubled to over US$2.57 trillion

76% increase in GDP per capita in current US$

- **2007:** $2,343
- **2014:** $4,155

In 2014, ASEAN economy was:
- **3rd** largest in Asia
- **7th** largest in the world

ASEAN POPULATION

- **3rd** largest in the world in 2014

<table>
<thead>
<tr>
<th>Region</th>
<th>Population</th>
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<tbody>
<tr>
<td>China</td>
<td>1,367 million</td>
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<tr>
<td>India</td>
<td>1,259 million</td>
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<tr>
<td>ASEAN</td>
<td>622 million</td>
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<tr>
<td>EU</td>
<td>504 million</td>
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<td>US</td>
<td>319 million</td>
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</tbody>
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More than **50%** of ASEAN's population is under 30 years old (compared to 39% of East Asia's and 34% of Europe's)

Source: ASEAN Secretariat (2015) A Blueprint for Growth ASEAN Economic Community 2015: Progress and Key Achievements
The ASEAN Economic Community (AEC) Blueprint is built on four interrelated and mutually reinforcing pillars:

1. **Single Market & Production Base**
   - Free Flow of Goods
   - Free Flow of Services
   - Free Flow of Investment
   - Free Flow of Capital
   - Free Flow of Skilled Labour
   - Priority Integration Sectors
   - Food, Agriculture & Forestry

2. **Competitive Economic Region**
   - Competition Policy
   - Consumer Protection
   - Intellectual Property Rights
   - Infrastructure Development
   - Taxation
   - E-commerce

3. **Equitable Economic Development**
   - SME Development
   - Initiative for ASEAN Integration

4. **Integration into Global Economy**
   - Coherent Approach towards External Economic Relations
   - Enhanced Participation in Global Supply Networks
AEC Scorecard Measures, Fully Implemented
ASEAN-wide and high-priority measures, by AEC Pillar, 2008-2015
Number of Measures (as at 31 October 2015)

| Single Market and Production Base | 256 | 21 | 92.4% |
| Competitive Economic Region      | 154 | 16 | 90.5% |
| Equitable Economic Development    | 100%|    |
| Integration into the Global Economy| 100%|    |

Source: ASEAN Secretariat (2015) A Blueprint for Growth ASEAN Economic Community 2015: Progress and Key Achievements
ASEAN Financial Integration Framework (AFIF)

In 2011, the ASEAN Central Bank Governors Meeting (ACGM) adopted The ASEAN Financial Integration Framework (AFIF) to integrate financial sector and market by 2020.

The AFIF aims to:
1) remove restrictions to the intra-ASEAN provision of financial services by ASEAN financial institutions;
2) build capacity and infrastructure to develop and integrate the ASEAN capital markets;
3) freer movement of capital across the ASEAN region;
4) harmonize payments and settlements systems; and
5) strengthen capacity building, regional financing arrangements, and regional surveillance.

• However, there is some flexibility. Each ASEAN Member State (AMS) has its own initial conditions; thus, each AMS may define its own milestones and timelines to achieve the common end goal of financial integration.
Governance structure of AFIF
In 2014, the ACGM endorsed the ASEAN Banking Integration Framework (ABIF) as a core component of ASEAN Financial Integration Framework (AFIF), and subsequently agreed to the Guidelines for its implementation.

- ABIF allows banks meeting certain criteria to have greater access to other ASEAN markets and more flexibility in operating there.
- ABIF is expected to support ASEAN economic integration by bringing greater competition among ASEAN banks, which would lead to emergence of strong pan-ASEAN regional banks with the scale and the capability to compete against the global banks.
The Guidelines are kept confidential but focus on the implementation of Qualified ASEAN Banks (QAB). Key points of the Guidelines are following:

a) QAB will be given national treatment in Host country in terms of market access and operational flexibility which is often not enjoyed by a foreign bank (e.g., opening of branches);

b) Financial soundness based on Basel capital accord, sizable market share in Home country and fit-and-proper of bank shareholders and management are key requirements;

c) Granting of QAB status is to be negotiated bilaterally based on a reciprocity principle.

d) In granting QAB status, Indigenous ASEAN banks with existing presence in AMSs are to be given priority.

e) ASEAN central banks aim to have concluded the first set of negotiations among ASEAN 5 by 2018 and among all AMS by 2020.

Currently MOU or LOI is exchanged between: Malaysia and Thailand; Malaysia and Philippines; Malaysia and Indonesia; Thailand and Indonesia.
AEC 2015 to 2025

AEC Blueprint 2025 (2016-2025)
- A Highly Integrated and Cohesive Economy
- A Competitive, Innovative and Dynamic ASEAN
- Enhanced Connectivity and Sectoral Cooperation
- A Resilient, Inclusive and People-Oriented, People-Centred ASEAN
- A Global ASEAN

- Single Market and Production Base
- Competitive Economic Region
- Equitable Economic Development
- Integration into the Global Economy

Current state of ASEAN Economic and Financial integration
No intra-ASEAN tariff

Figure 1.2 Trend of the Intra-ASEAN average tariff rate, 2000-2013

Source: ASEAN Tariff Database

Source: ASEAN Secretariat (2014) ASEAN Community in Figures – Special Edition 2014
Trade integration

Major Trading Partners

24% 15% 11% 10% 9%

Intra-ASEAN trade comprised the largest share of ASEAN’s total trade by partner in 2015.

Trend of ASEAN Trade with ASEAN+3, ASEAN+6 and EAS (in US$ billion), 1993-2013

Source: ASEAN Community in Figures – Special Edition 2014
As the characteristics of East Asia by export destination,
• Exports within the East Asian region are centered on those of intermediary goods.
• Exports to NAFTA and EU are predominantly those of final goods, especially consumption goods.

Source: R I E T I - T I D  2 0 1 1
Trend in the export amount of consumption goods in East Asia by counterpart country

(Billion dollars)

Asian currency crisis
(1997)

Failure of Lehman Brothers
(2008)

East Asia

EU27

U.S.

Japan

ASEAN

China

Hong Kong

Taiwan

South Korea

Note: East Asia consists of Japan, China, South Korea, Hong Kong, Taiwan, Brunei, Cambodia, Indonesia, Malaysia, Philippines, Singapore, Thailand and Vietnam.

Source: RIETI-TID 2011.


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Who is lending to Asia?

Note: Remolona, E. & Shim, I. 2015 The rise of regional banking in Asia and the Pacific, BIS Quarterly Review September 2015
But ASEAN banks’ share is still small

Market share of the three largest creditor countries

“The increase in concentration was pronounced for Indonesia, Korea, Malaysia, New Zealand, the Philippines and Thailand. For these six borrowing countries as a group, the five largest creditors in the first quarter of 2015 included three economies from the region – Australia, Japan and Singapore – besides the United Kingdom and the United States. In 2007, the list of the five largest creditors had included France and Germany instead of Australia and Singapore. As of the first quarter of 2015, Japan was the most important creditor for Indonesia and Thailand, and Singapore for Malaysia.”

Note: Remolona, E. & Shim, I. 2015 The rise of regional banking in Asia and the Pacific, BIS Quarterly Review September 2015
Current state of ASEAN Integration (in summary)

- Intra-ASEAN trades is still small comparing to EU.
- However, Intra-regional trades within ASEAN+3 is comparable to EU.
- Intra-East Asia’s trade is large, but final destination is outside of the region. higher.
- However, East Asia, particularly China and ASEAN, are growing rapidly and East Asia is become the biggest final destination of trade.
- Banking within ASEAN is rather limited.
- However, Asia-Pacific banks are far much more dominant.

- It is better to broaden the scope of regional integration from ASEAN to ASEAN+3 and ASEAN+6.
- ASEAN can leverage its position by pursuing open regionalism
What needs to be done?
Is EU a model for ASEAN?

• EU is
  – Fully integrated market, with
    • the single market
    • under the same regulations and directives
    • Unified supervisory bodies
      – European Banking Authority
      – European Securities Authority
      – European Insurance and Pension
    • The Single Resolution Mechanism

• ASEAN needs to seek its Financial Integration model
  – each AMS may define its own milestones and timelines to achieve the common end goal of financial integration.

• But how?
Strategies included in AEC Blueprint 2025
- 2015ASEAN 2025: Forging Ahead Together-

• Para 17. i: “Strengthen financial integration to facilitate intra-ASEAN trade and investment by increasing the role of ASEAN indigenous banks, having more integrated insurance markets, and having more connected capital markets “

• Para 17.i.b: “Provide greater market access and operational flexibility for Qualified ASEAN Banks (QABs) through the ASEAN Banking Integration Framework (ABIF), based on each country’s readiness and on a reciprocal basis, thereby reducing gaps in market access and operational flexibility across ASEAN”

• Para 17.i.c: “Promote deeper penetration in insurance markets through the ASEAN Insurance Integration Framework (AIIF), with greater risk diversification, deeper underwriting capacity, improved and strengthened insurance sector supervision and regulatory frameworks”

• Para 17.i.d: “Further deepen and interlink capital markets by progressing towards more connectivity in clearing settlement and custody linkages to facilitate investment in the region, and allow investors and issuers to tap cross-border ASEAN capital markets efficiently, in line with the objective of ASEAN Capital Market Infrastructure (ACMI) Blueprint. “

• Para 17.i.e: “Promote the development of sovereign bond markets as well as corporate issuances that will diversify risks from the banking system and provide savers with greater opportunities to invest“
Financial stability measures explained in the AEC Blueprint

- Para 17.3.a: “Intensify the existing process of macroeconomic and financial surveillance through identifying financial system risks and vulnerabilities, and intensifying exchange of key macroeconomic information among monetary and fiscal authorities”

- Para 17.3.b: “Further enhance cross-border cooperative arrangements in relation to the implementation of the ABIF with the emergence of regionally active banks during both crisis and in the normal course of business. In the near term, existing regional and bilateral cooperation platforms for macro-surveillance and supervision will continue to perform an integral role.
  - ASEAN+3 Macroeconomic Research Office (AMRO)
  - EMEAP

- Furthermore, closer dialogues between authorities may be achieved through regional supervisory colleges”

- Para 17.3.c: “Make prudential regulations more cohesive, aimed at achieving greater consistency with international best practices and regulatory standards”
The measures for the key cross-cutting areas under the AEC Blueprint

• Capital account liberalization
  – . i. a: “Ensure an orderly capital account liberalisation”

• Payment and Settlement Systems
  – promoting standardisation
  – developing settlement infrastructure for cross-border trade, remittance, retail payment systems and capital markets.
  – This will provide an enabling environment to promote regional linkages and payment systems that are safe, efficient and competitive.
  – This will also require a certain level of harmonisation of standards and market practices based on international best practices (such as ISO 20022) to foster stability and efficiency within as well as outside the region.

• Capacity building
  – narrow the financial development gap in the region. This can be achieved through the conduct of learning programmes and exchanges of knowledge and experiences, and best practices in areas relevant to financial integration and development,
ASEAN+3 Asian Bond Markets Initiatives (ABMI)

(Chairman's Press Release on the Asian Bond Markets Initiative, 7 August 2003)

• ABMI aims to develop efficient and liquid bond markets in Asia, which would enable **better utilization of Asian savings for Asian investments**.
• The ABMI would also contribute to the **mitigation of currency and maturity mismatches** in financing.

- ABMI contributes to financial stability by creating multiple channels of financing.
Major outputs of ABMI

Research on:
- Infra bond finance
- Broadening the investor base
- CSD-RTGS Linkages as regional safety-net

Harmonization and standardization
- ASEAN+3 Multi-currency Bond Issuance Framework (AMBIF)

CGIF
$700 million

Asian Bonds Online

CSIF
CBs
CSDs

ABMF
Public Private platform
Evolution of ABMI

Global Financial Crisis

Stronger economic linkages and synchronization of markets

Bond markets as a spare tire.

Promoting development of domestic markets

Bond markets as another wheel.

Linking the fragmented markets to be more resilient regional capital markets

Financial regulatory overhaul

More integrated financial markets

ASEAN financial integration + PRC, JPN, KOR

New regional safety net

CSD-RTGS Linkages

CMIM ($120 Billion) + AMRO = Macroeconomic stability in crisis
ABMI: additional intermediary channel, local currency liquidity, LCY bond as collateral
= Micro financial system stability in peace time
Remaining issues for financial stability

• Development of institutional safety-net in all ASEAN member states
  – Deposit Insurance
  – Insurance policy holders protection
  – Cross-border collateral and repo

• Coordination among regulators not only among ASEAN but also ASEAN+3 or +6
  – Prevention of regulatory arbitrage
  – Information sharing through supervisory college
  – Cross-border resolution mechanism
Supervisory College

- Colleges are permanent, although flexible, coordination structures that bring together regulatory authorities involved in the supervision of a banking group. In practice, colleges are a mechanism for the exchange of information between home and host authorities, for the planning and performance of key supervisory tasks in a coordinated manner or jointly, including all aspects of ongoing supervision, and also for the preparation for and the handling of emergency situations.

- One of the fundamental tasks for supervisory authorities as members of colleges is reaching joint decisions on the risk-based capital adequacy of cross-border groups and their EEA subsidiaries.

Source: EBA website
Challenges

• Need for regional voice presented to the international standard setting bodies
• Regional coordination under different level of market developments
  – Institutional safety-nets must be developed.
• Participation in supervisory colleges of GSFIs

• Can ASEAN leverage its position in ASEAN+3(or 6) to influence international standard setting discussion?
  – EMEAP WG on Banking Supervision (WG/BS)
Thank you

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