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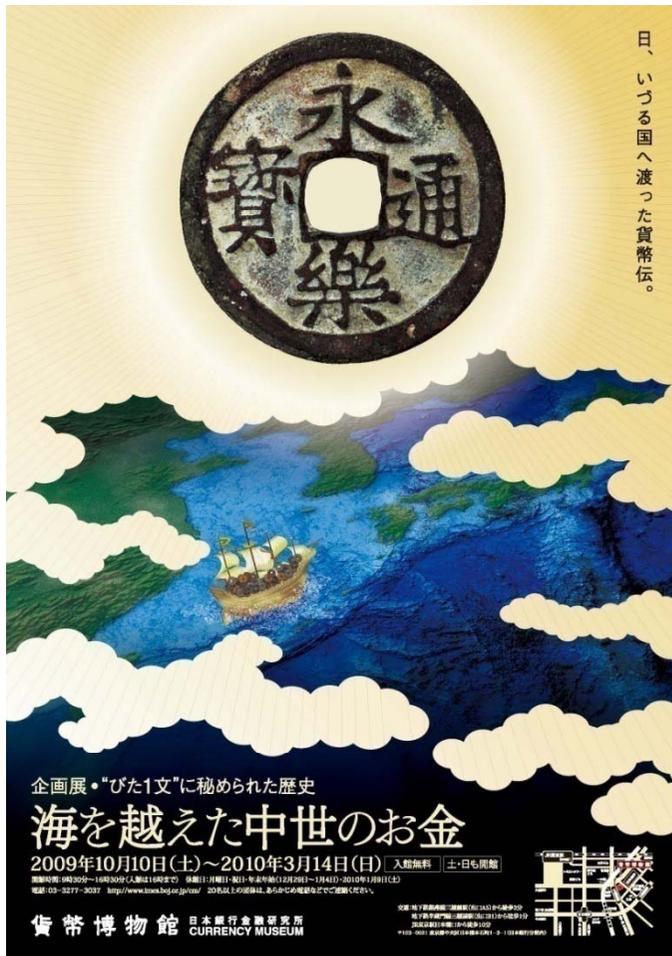
Session 1, Asian Financial Collaboration

# Financial Cooperation in East Asia and Its Future Direction

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The views expressed in this presentation are those of the author and do not necessarily reflect the views of the Bank of Japan.

# Asia's First Common Currency?



- An Asian common currency: an impossible dream?
- But a common currency in East Asia is not new.
  - *Eiraku-sen* (永樂錢)
  - 15th century (明 永樂帝) Ming Dynasty
- China was a dominant economic power.
- There were common merchant rules and practices, and a currency was credible.

# My Argument (1/2)

- With the progress of globalization, regional integration (regionalization) becomes increasingly important.
  - After successful integration and institutionalization, the EU is increasing its influence on the formation of an international architecture.
- Achievements can be seen in economic integration. In East Asia, *de facto* economic integration has progressed in trade and production network.
  - But institutionalization lags behind.
  - East Asia needs to improve its financial services to support economic integration.

# My Argument (2/2)

- A two-track approach -- (a) currency arrangements + (b) financial integration -- should be pursued.
  - a) Institutionalization or *de jure* integration should be advanced, but this will take time.
  - b) A pragmatic approach should be adopted for financial integration.
- a) For currency arrangements, the provision of liquidity is an important task.
- b) For financial integration, we should focus on the beneficiaries and invite initiatives from the private sector.

# a) Currency Arrangements and/or b) Financial Integration

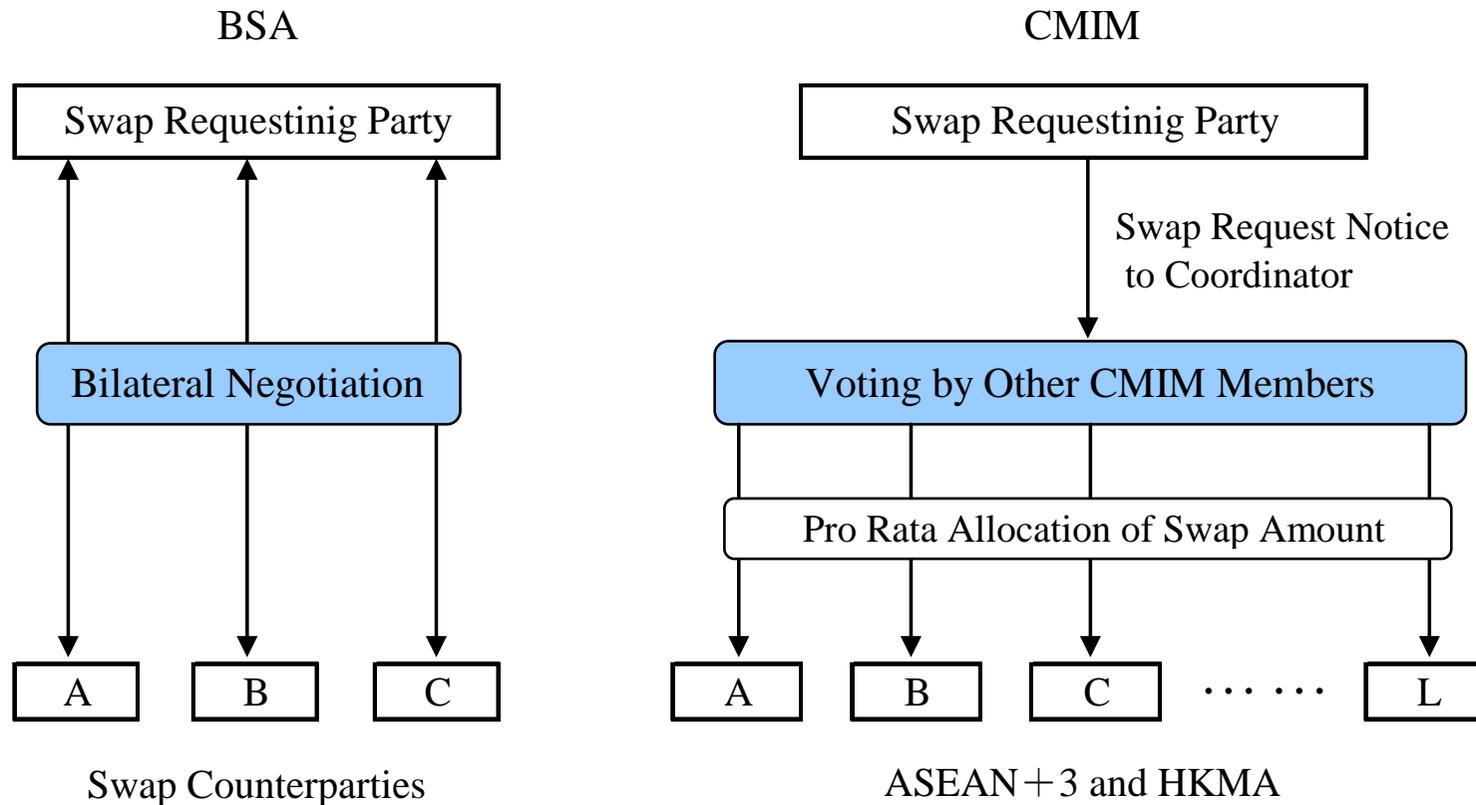
- Ultimate target: a) a single currency and/or b) a single market.
  - a) common currency, basket currency (ACU) . . .
  - b) harmonization of financial infrastructures (payment systems, legal frameworks, business practices/rules, corporate governance . . .)
- a) and b) are complementary.
  - b) is a necessary condition for a).
  - But a) is a difficult issue and may take a long time to achieve.
    - Different (monetary policy) frameworks (e.g., China and Japan)

# Experiences in Asia

- Achievements: 1) Chiang Mai Initiatives (CMIM: Figure 1) and 2) Asian Bond Markets Initiatives (ABMI)/Asian Bond Fund (ABF: Figure 2)
  - New Miyazawa Initiatives, Asian Monetary Fund . . . AMRO (The ASEAN+3 Macroeconomic and Research Office)
  - The ABF increased momentum in cooperation.
    - Concrete achievement is important.
- But there is too much emphasis on “crisis solution and prevention.”
  - In comparison to trade and investment, financial integration to improve financial services lags behind.

# Fig 1. CMIM Characteristics in Comparison with BSA

- Major progresses of CMIM
  - Promptly activated through collective decision making process.



## Fig.2 Asian Bond Fund (ABF) Projects

	ABF1	ABF2
Start of Investment	July 2003	March 2005
Investment Style	Passively managed against designated benchmark indices	
Qualifying Assets	<ul style="list-style-type: none"> <li>• Sovereign and quasi-sovereign bonds issued in eight EMEAP economies</li> <li>• Denominated in USD</li> </ul>	<ul style="list-style-type: none"> <li>• Sovereign and quasi-sovereign bonds issued in eight EMEAP economies</li> <li>• <b>Denominated in domestic currencies</b></li> </ul>
Fund Manager	Bank for International Settlements	Private Fund Managers (one for each fund)
Investors	EMEAP central banks only	Phase 1: EMEAP central banks only Phase 2: EMEAP central banks and <b>other public and private sector investors</b>

# Focus on Financial Integration

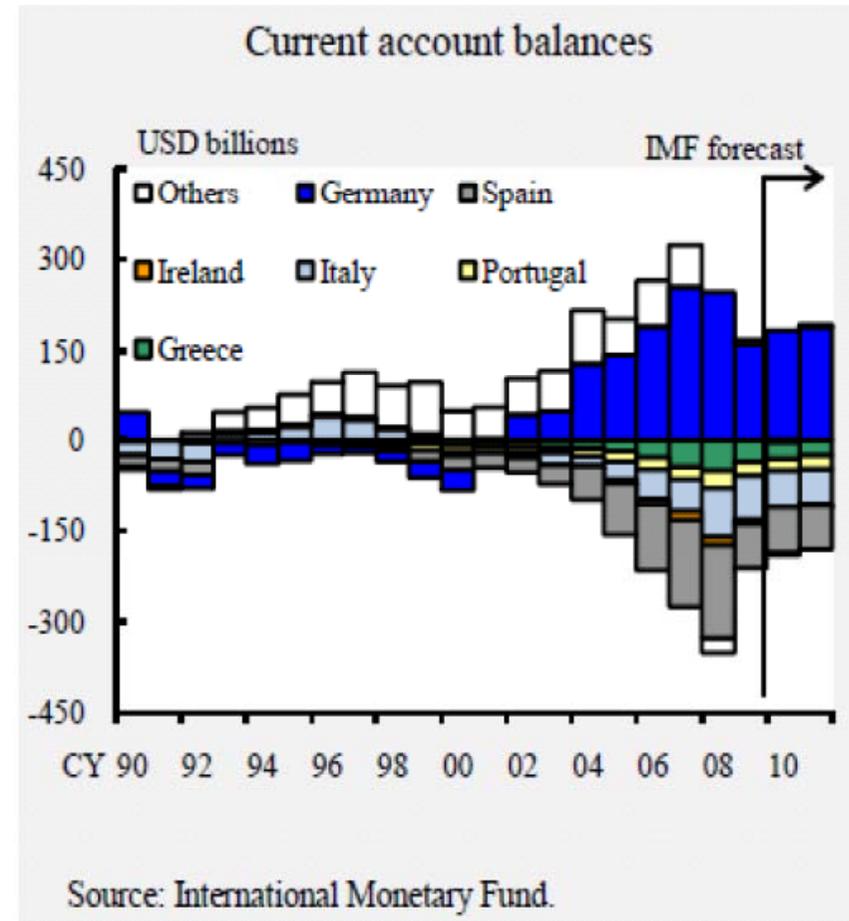
- Firms are requiring improved financial services (e.g., borderless and “seamless” financial services, and CMS [cash management services]).
  - Establishment of good payment services and harmonization of business practices (legal framework, corporate governance) are important.
  - Some proposals for payment services have been presented by Japanese academics: Nakakita (2010)’s “bottom-up approach.”
  - The Group of Experts (ABMI Task Force 4) presented a proposal for securities settlement.

# Lessons from Europe (1/2)

- The single currency of the euro is well known, but a lot of progress in a single financial (monetary and capital) market.
- A systematic process
  - The 1996 Giovannini Group
  - The 1998-2005 Financial Service Action Plan
  - External evaluation + internal review

# Lessons from Europe (2/2)

- Achievements
  - Micro level: efficient service (reduction in transaction and capital costs)
  - Macro level: adjustment in the current account
    - The Greek crisis



# What Should We Learn from Europe?

- A two-track approach
  - A single currency and a single market
- A systematic process
- A grand design,
  - 1) a clear goal, 2) a roadmap, and 3) a review process
- Private initiatives
  - Academia, business

# Future Direction

## a) Move forward to a single market

- Necessity for a grand design and private initiatives
  - Single currency: coordination among authorities
  - Single market: private initiatives, business opportunities

## b) Establish liquidity facilities

- AMRO (The ASEAN+3 Macroeconomic and Research Office) is a promising step.
- Establish a “club” in the Central Bank society.

# Reservations

- Cooperation is most important.
  - Human networks, reliable relations, exchanges of views and information
- A single currency is not a “magic wand.”
  - Although the euro has been introduced, Europe has not been immune from the current crisis.
  - Global dollar funds supplying operations (swap) demonstrate the central role played by the Federal Reserve.
  - Forming currency arrangements is a difficult task.

# Conclusions

- East Asia must move forward to achieve financial integration (single market/market integration) as well as currency arrangements.
- With financial integration, East Asia can provide better financial services for firms operating cross-border businesses in the region.
- East Asia can invite private initiatives from the financial sector in the region. In this way, it can enhance development in the financial industry.
- This will promote a single currency, since a smoothly functioning financial market is the basis for a key international currency.

# Ref 1) Definition of Financial Integration by ECB

First, the ECB has adopted a definition of financial integration: it considers the market for a given set of financial instruments or services to be fully integrated when all potential market participants in such a market

- (i) Are subject to “a single set of rules” when they decide to deal with those financial instruments or services,
- (ii) have equal access to this set of financial instruments or services, and
- (iii) are treated equally when they operate in the Market

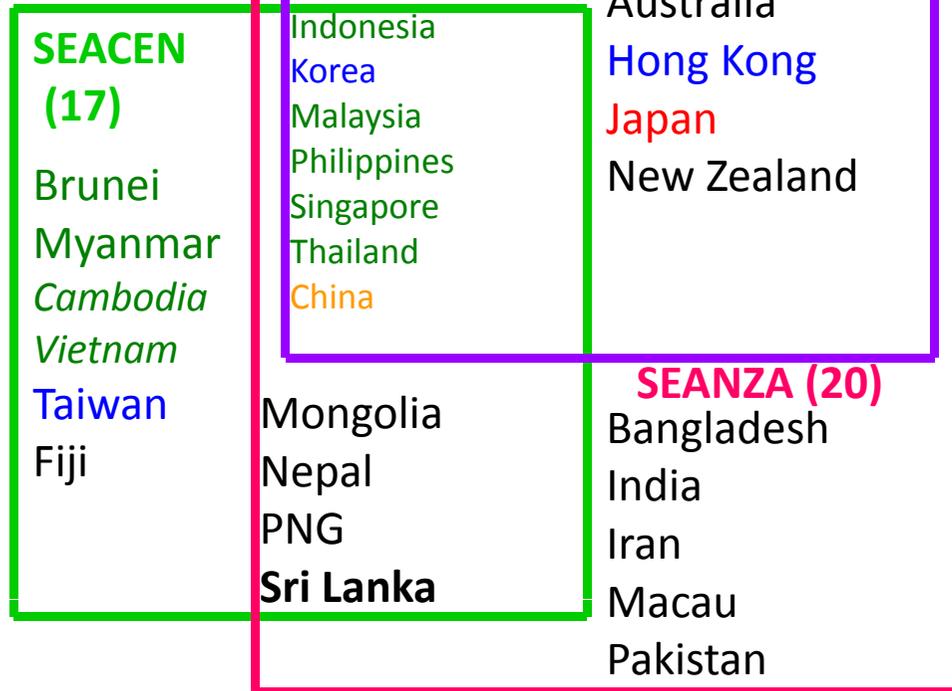
(source) ECB “Financial integration in Europe” March 2007

## Ref 2) The Role of Eurosystem in the financial Integration

- the Eurosystem contributes to furthering the financial integration process in four main ways:
    - (i) giving advice on the legislative and regulatory framework for the financial system and on direct rule-making;
    - (ii) acting as a catalyst for private sector activities by facilitating collective action;
    - (iii) Enhancing knowledge, raising awareness and monitoring the state of European financial integration; and
    - (iv) providing central bank services that also foster European financial integration
- (source) ECB “Financial integration in Europe”  
March 2007

# Ref 3) cooperation forums in Asia

☆ central  
bank cooperation



☆ Government + central  
bank cooperation in Asia

ASEAN + 3 ··· ASEAN + Japan, China, Korea

ASEAN ··· Indonesia, Malaysia, Philippines,  
Singapore, Thailand, Brunei,  
Myanmar, Cambodia, Laos, Vietnam

**SEANZA ··· South East Asia, New Zealand and Australia (20)**

(founded in 1956 by 5 original member central banks: Australia, India,  
New Zealand, Pakistan and **Sri Lanka**)

**SEACEN ··· South East Asian Central Banks (17)**

(founded in 1982 by 8 original member central banks: Malaysia, Indonesia,  
Myanmar, Nepal, Philippines, Singapore, **Sri Lanka**, Thailand)

# Main References

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- Takahashi, Wataru. “The East Asian economies after the financial crisis: a role for the Japanese yen?” In H. Dobson and G.Hook ed. Japan and Britain in the Contemporary World : Response to Common Issues (Sheffield Centre for Japanese Studies/ Routledge Series), Routledge Curzon, May 2003