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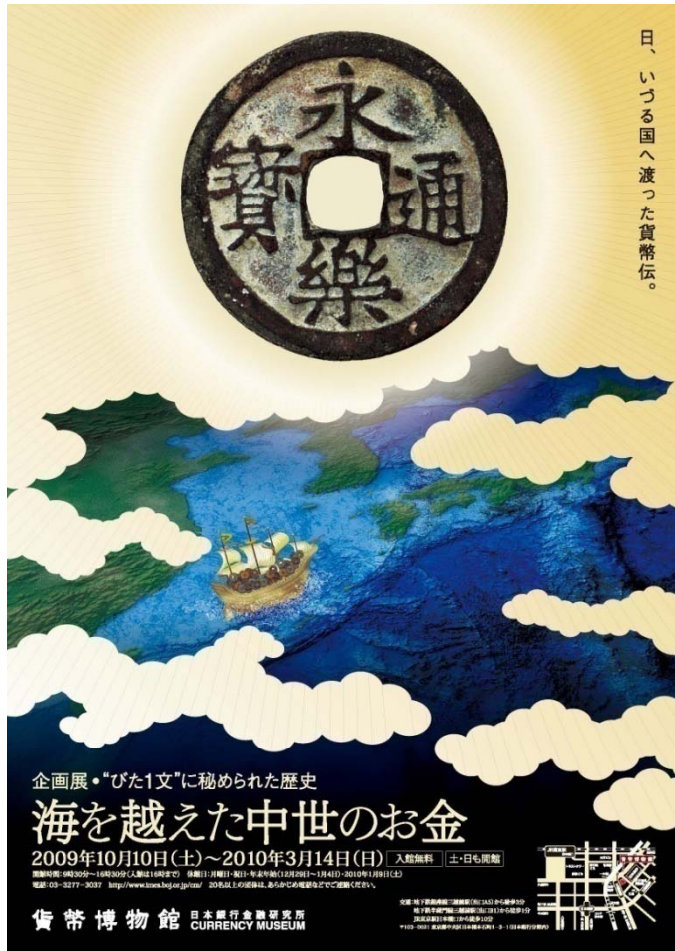
Session 1, Asian Financial Collaboration

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.

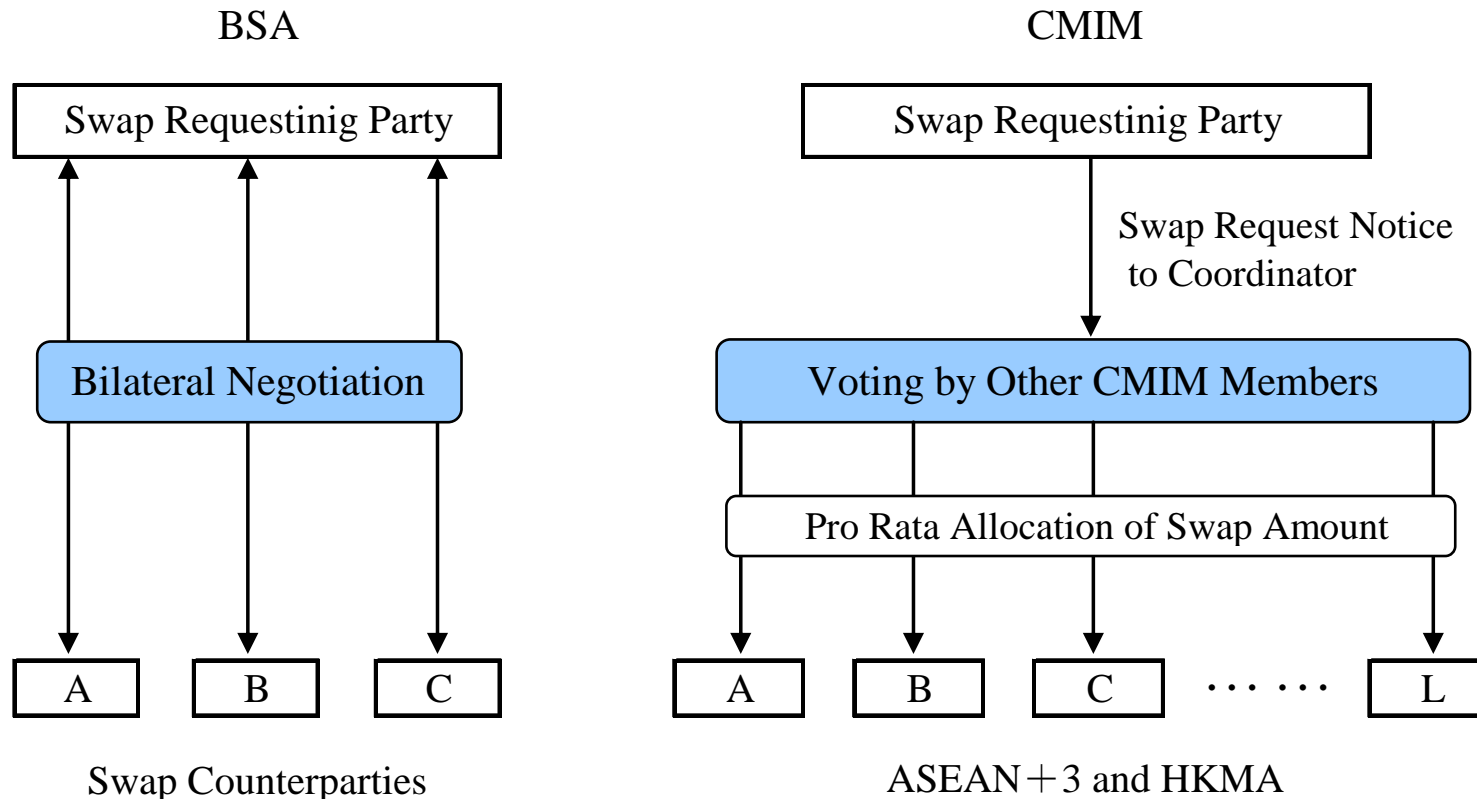


Fig.2 Asian Bond Fund (ABF) Projects

	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"> • Sovereign and quasi-sovereign bonds issued in eight EMEAP economies • Denominated in USD 	<ul style="list-style-type: none"> • Sovereign and quasi-sovereign bonds issued in eight EMEAP economies • Denominated in domestic currencies
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 other public and private sector investors

Focus on Financial Integration

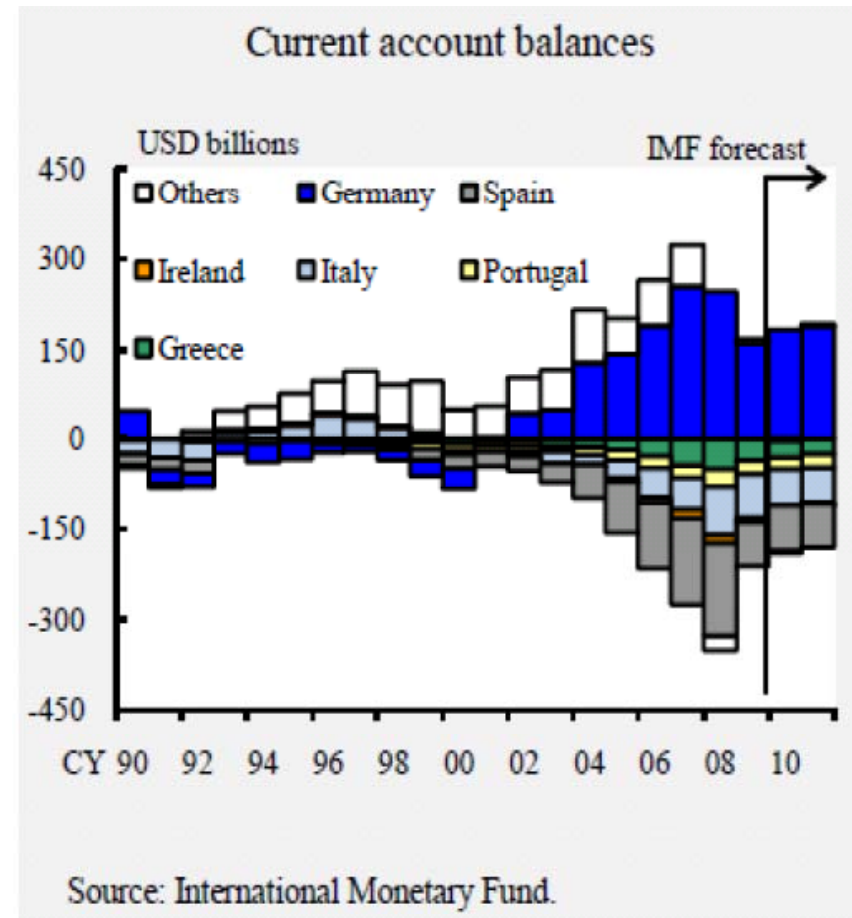
- Firms are requiring improved financial services (e.g., borderless and “seamless” financial services, and CMS [cash management services]).
 - Establishment of good payment services and harmonization of business practices (legal framework, corporate governance) are important.
 - Some proposals for payment 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

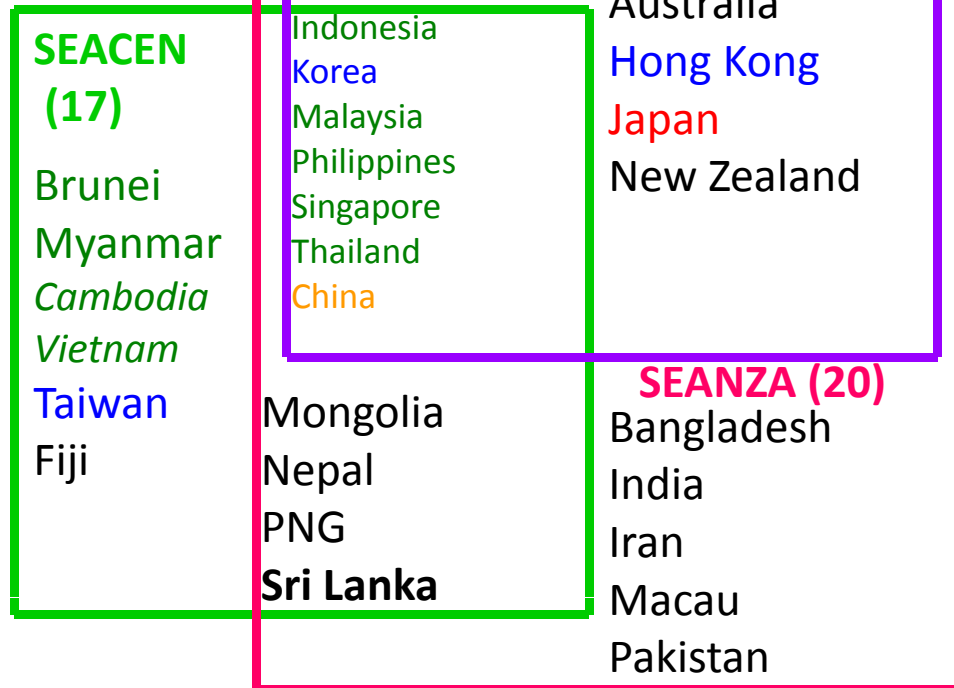
Ref 2)The Role of Eurosystem in the financial Integration

- 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