

ASEAN Capital Market Integration and Lessons from the European Union

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Outline

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- ASEAN Capital Market Integration
 - Banking
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Introduction

- Integration in ASEAN have been driven more by market forces rather than institutions.
- Region's economies have pursued export-led growth strategy. They have generally been open to trade and FDI from abroad.
- Trade Integration started early but financial integration catching up
- Economies have been removing barriers to capital flows and liberalizing their current accounts.

Stages of Integration

1. Free Trade Area
2. Customs Union
3. Common Market
4. Economic Union
 - Banking Union
 - Fiscal Union
 - Monetary Union
5. Political Union

ASEAN Capital Market Integration

- Impetus was the 1997/98 Asian financial crisis which exposed the currency and maturity mismatch endemic in the region's financial system.
- Banks were borrowing short-term in foreign currency (usually US\$) and lending it in local currency long-term.
- Authorities recognize the need to develop stronger and more robust regional financial markets to prevent a repeat of the crisis.




Financial integration lags behind trade

- While trade within the region is now mostly free of barriers, there are still significant barriers towards accessing each other's capital markets.
- Different rules and regulations make it difficult for investors to invest in their neighboring countries.
- However there are concerted efforts among the ASEAN+3 economies to further promote greater integration of financial markets.
- Over time, we expect the gap between financial to gradually catch up.

Banking Integration

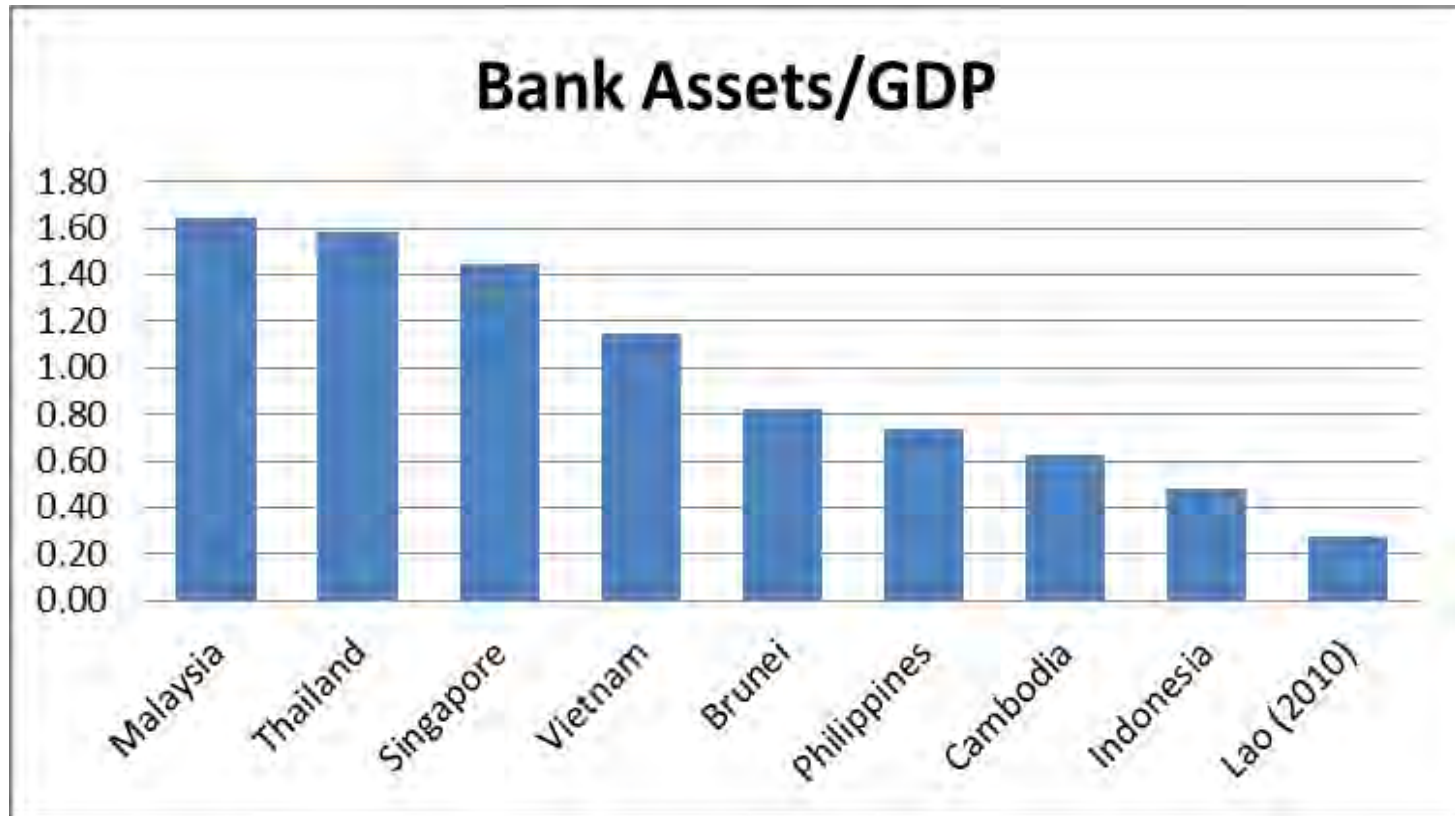
- Banks are the most important financial institutions in ASEAN.
- So far, there has been little integration in the ASEAN banking sector.
- Non-regional banks (Standard Chartered, ANZ, MUFG) have larger footprint in ASEAN than regional ASEAN banks.

Banks' presence in the region

Number of countries present		Number of countries present (excluding home countries)	
	10		8
	9		7
	8		7
	8		6
	8		5
	7		2
	6		1

Note: Includes branch, representative office and subsidiary.
Also includes recently issued banking licenses from Myanmar

Banking Sector Development Varies



Source: IMF International Financial Statistics.
Singapore, Vietnam and Lao data using old IFS reporting format

Malaysian and Singapore banks largest



Source: Bloomberg

Top 3 banks by asset size (ASEAN 6)

Indonesia	BANK MANDIRI
	BANK RAKYAT INDONESIA
	BANK CENTRAL ASIA
Malaysia	MALAYAN BANKING BHD
	CIMB GROUP HOLDINGS BHD
	PUBLIC BANK BHD
Philippines	BDO UNIBANK INC
	METRO BANK & TRUST CO
	BANK OF THE PHILIPPINE ISLANDS
Singapore	DBS GROUP HOLDINGS LTD
	OVERSEA-CHINESE BANKING CORP LTD
	UNITED OVERSEAS BANK LTD
Thailand	BANGKOK BANK PUB
	SIAM COMM BK PCL
	KRUNG THAI BANK
Vietnam	VIETNAM JS COMMERCIAL BANK FOR INDUSTRY AND TRADE
	*BANK FOR FOREIGN TRADE OF VIETNAM JSC
	*MILITARY COMMERCIAL JS BANK

*Several data not available for Vietnam's rank 2 bank

Indonesian banks most profitable



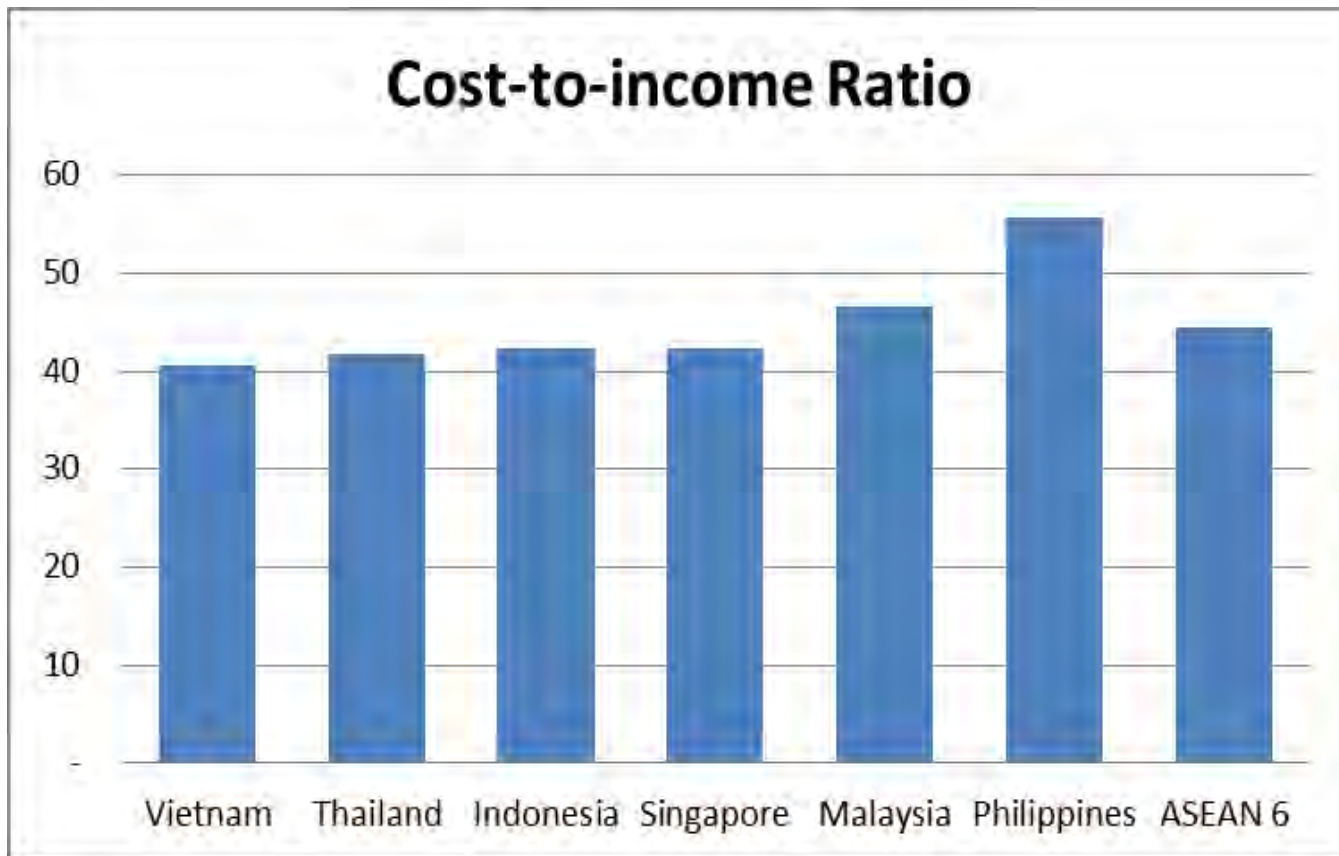
Source: Bloomberg

Interest margin highest in Indonesia



Source: Bloomberg

Philippines banks have high cost



Source: Bloomberg

Promoting Banking Integration

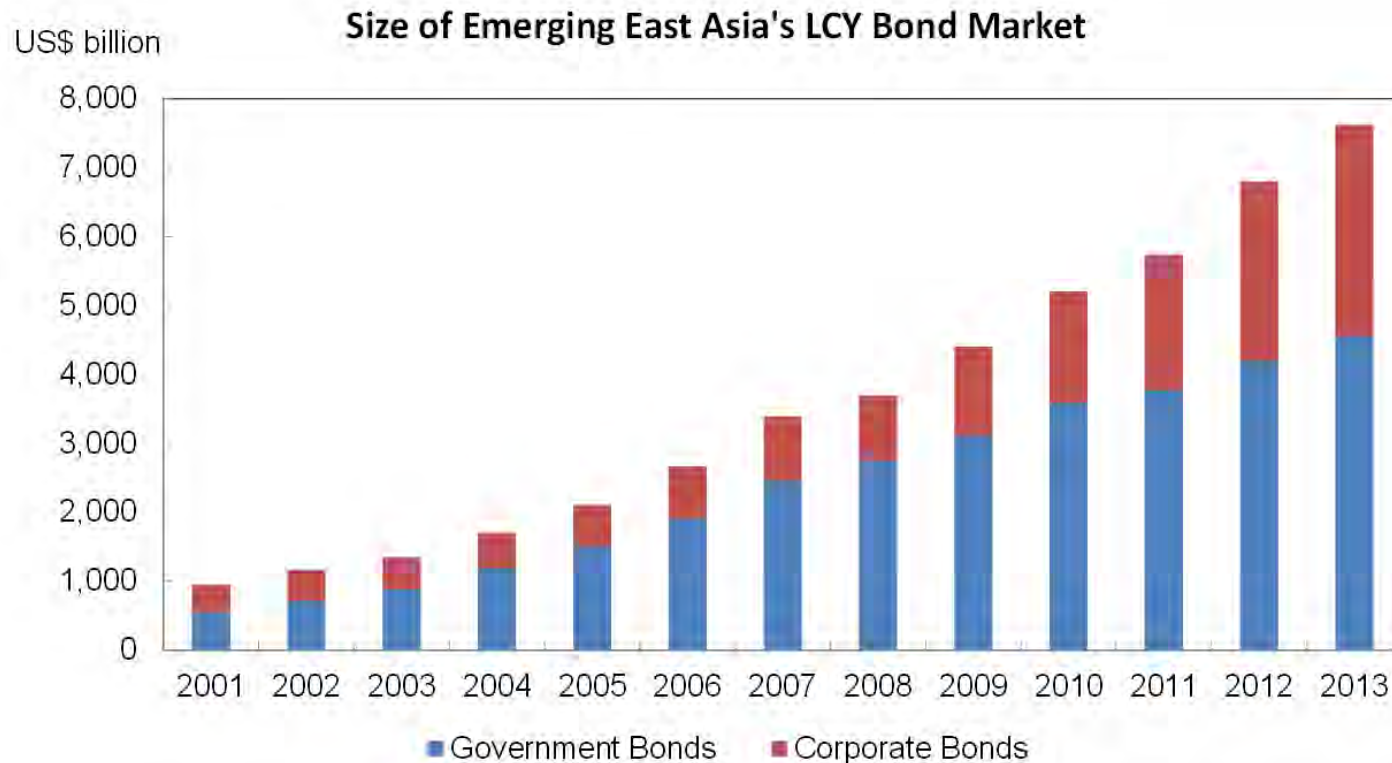
- An integrated financial market requires participants to operate under a common set of rules and regulations.
- Greater integration in ASEAN would require a move towards harmonizing rules and regulations.
- But diversity in the financial development of ASEAN countries is hampering that.
- ASEAN Banking Framework is working to facilitate Qualified ASEAN Banks (QABs) entry into domestic banking markets.

Bond and Equity Market Integration

- Local Currency (LCY) bond market has grown tremendously since 2001.
- While government bonds have a bigger share of the market, corporate bonds are catching up.
- Malaysia, Singapore and Thailand all have well developed bond markets.
- Growing interest by foreign investors to invest in ASEAN bond markets.

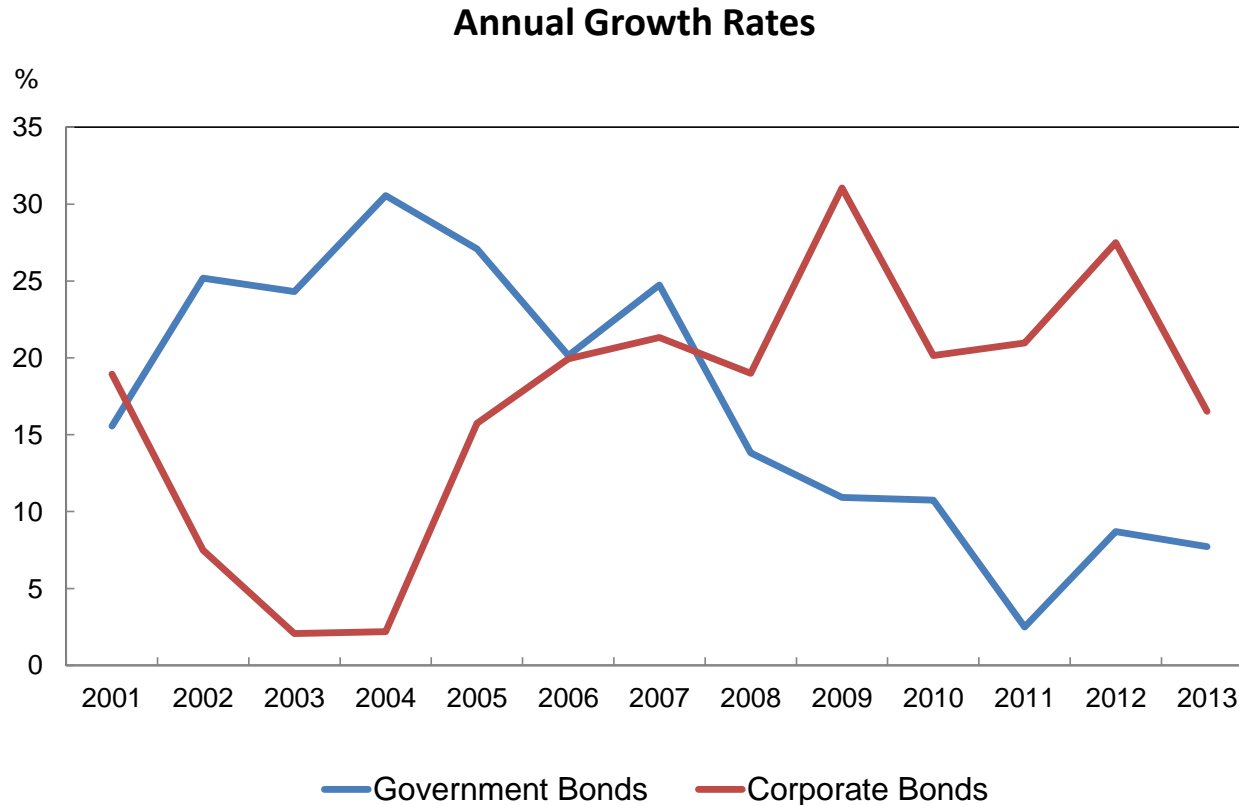
Rapid growth in LCY bonds

Emerging East Asia's LCY bond market reaches US\$7.6 trillion at end-2013



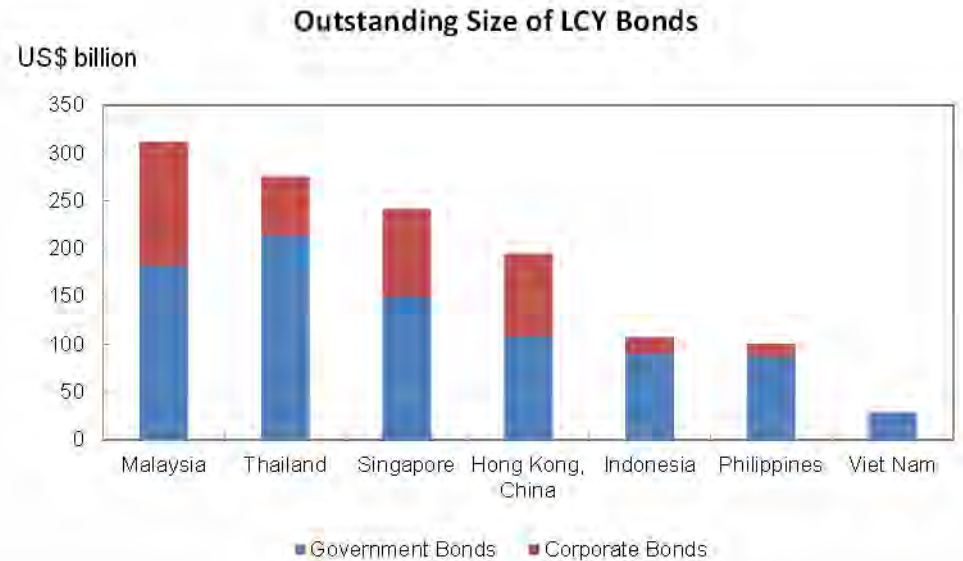
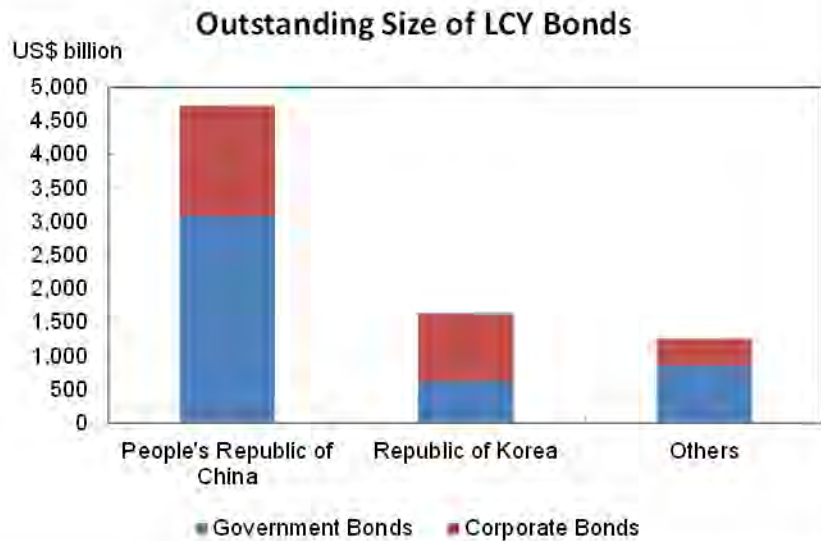
Note: Emerging East Asia refers to the People's Republic of China; Hong Kong, China; Indonesia; the Republic of Korea; Malaysia; Philippines; Singapore; Thailand; and Viet Nam.
Source: AsianBondsOnline.

Corporate bond market rising faster than government bond market



Note: Growth figures are based on end-December 2013 currency exchange rates and do not include currency effects.

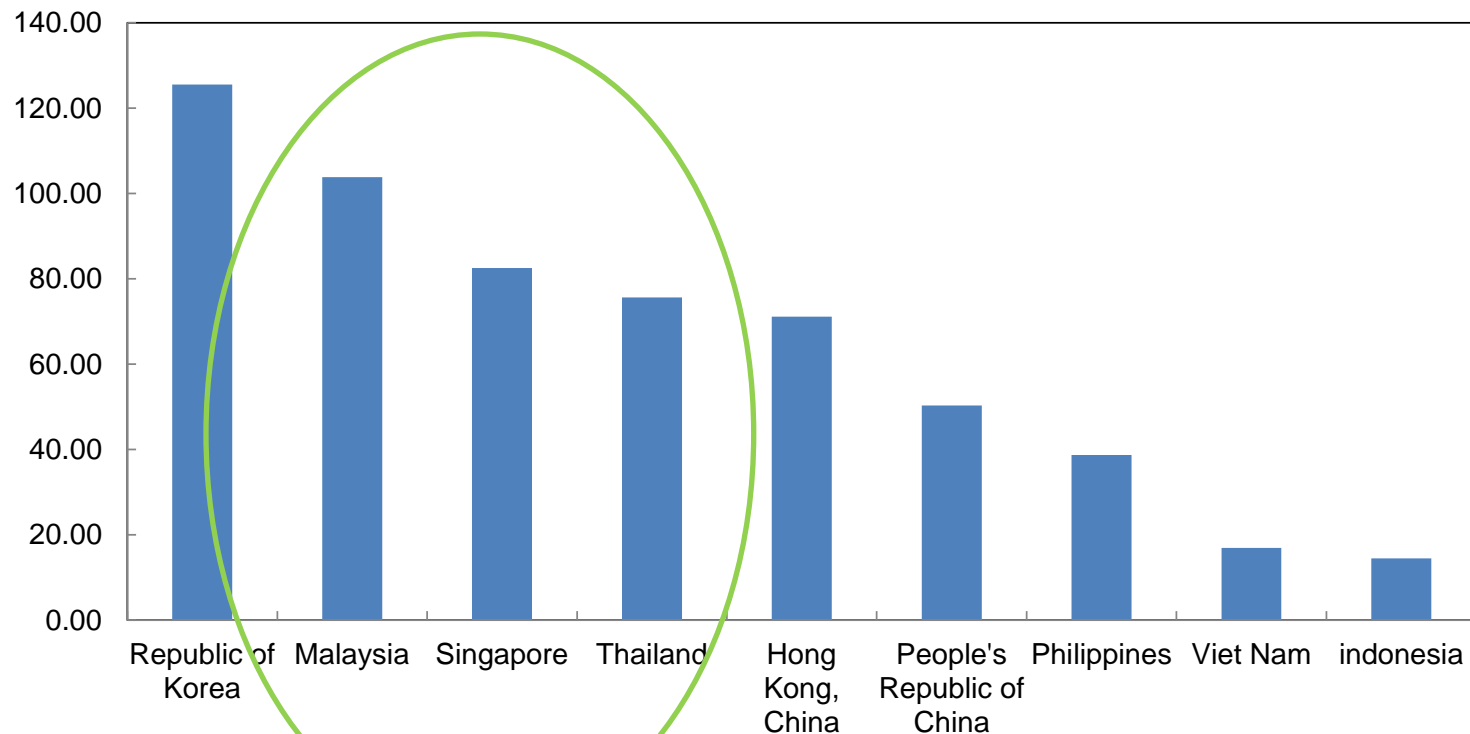
PRC is the largest LCY bond market in the region



Note: Data as of end-2013.
Source: AsianBondsOnline.

Malaysia, Singapore and Thailand have well developed bond markets

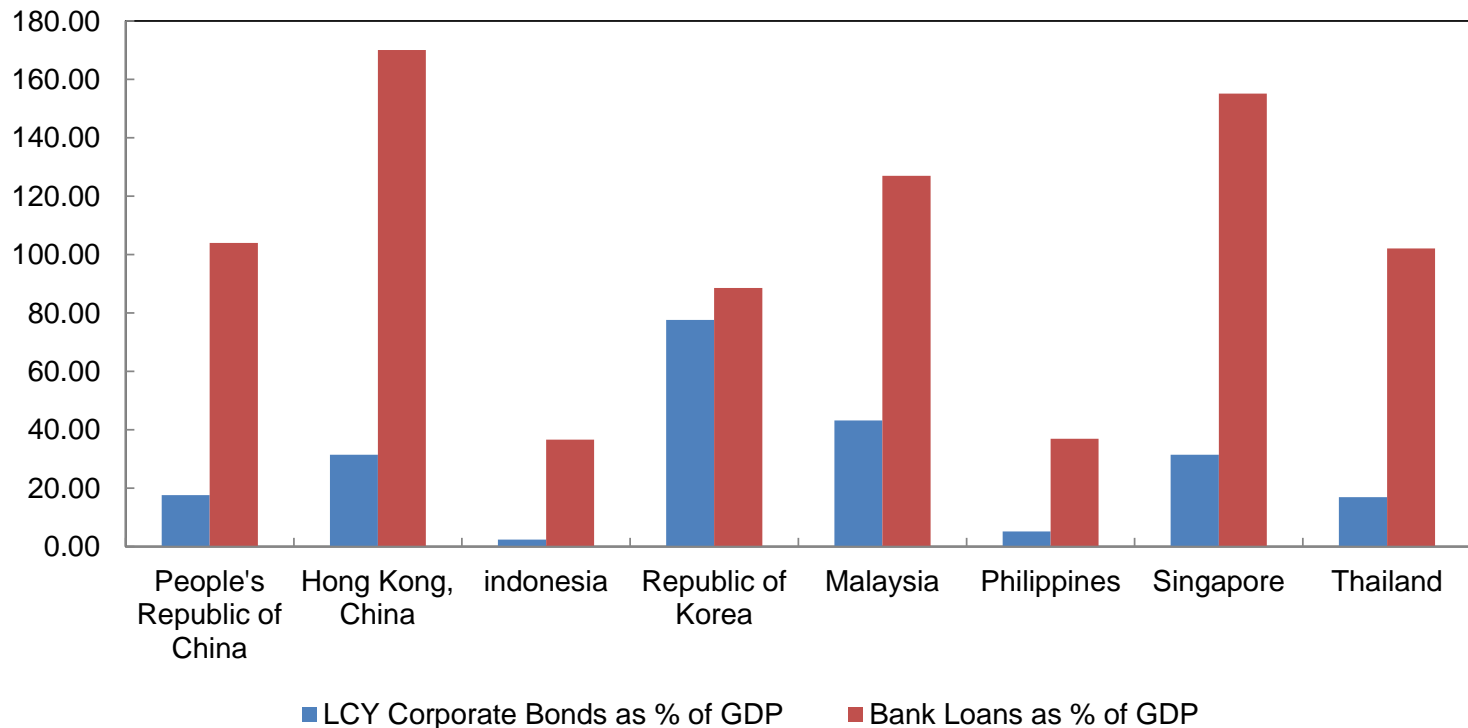
LCY Bonds as a Share of GDP



Note: Data as of end-2013.
Source: AsianBondsOnline.

Bank loans are still the major source of debt financing

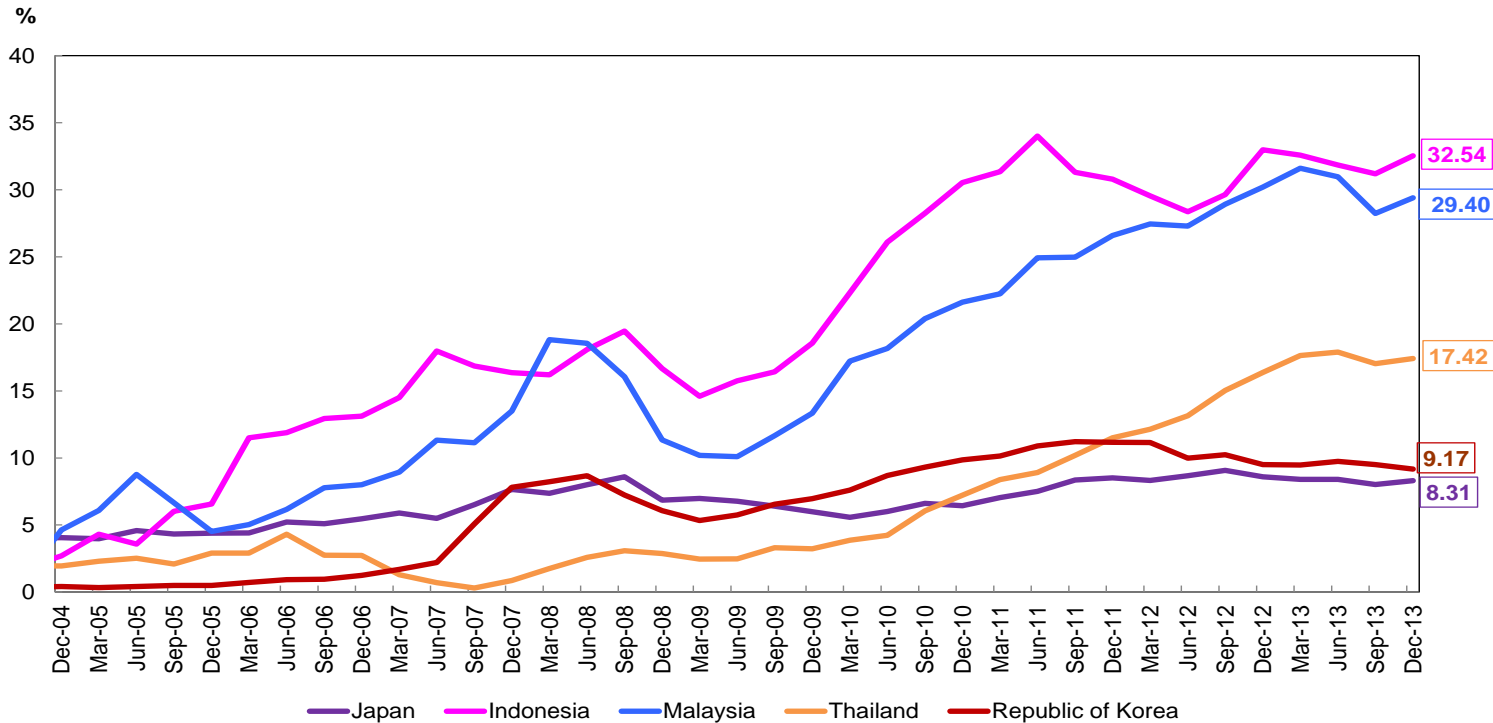
LCY Corporate Bonds and Bank Loans as % of GDP



Note: Data as of end-2013.
Source: AsianBondsOnline.

Growing foreign interest in Indonesian, Malaysian and Thai bond markets

Foreign Holdings of LCY Government Bonds



Asian Bond Market Initiative

- Asian Bond Markets Initiative (ABMI) was started in 2003 to promote the development of local currency bond markets in Asia among ASEAN+3 countries.
- Asian Bonds Online.
 - <http://asianbondsonline.adb.org/>
- Asia Bond Monitor.
 - <http://asianbondsonline.adb.org/regional/abm.php>

Asian Bond Market Forum

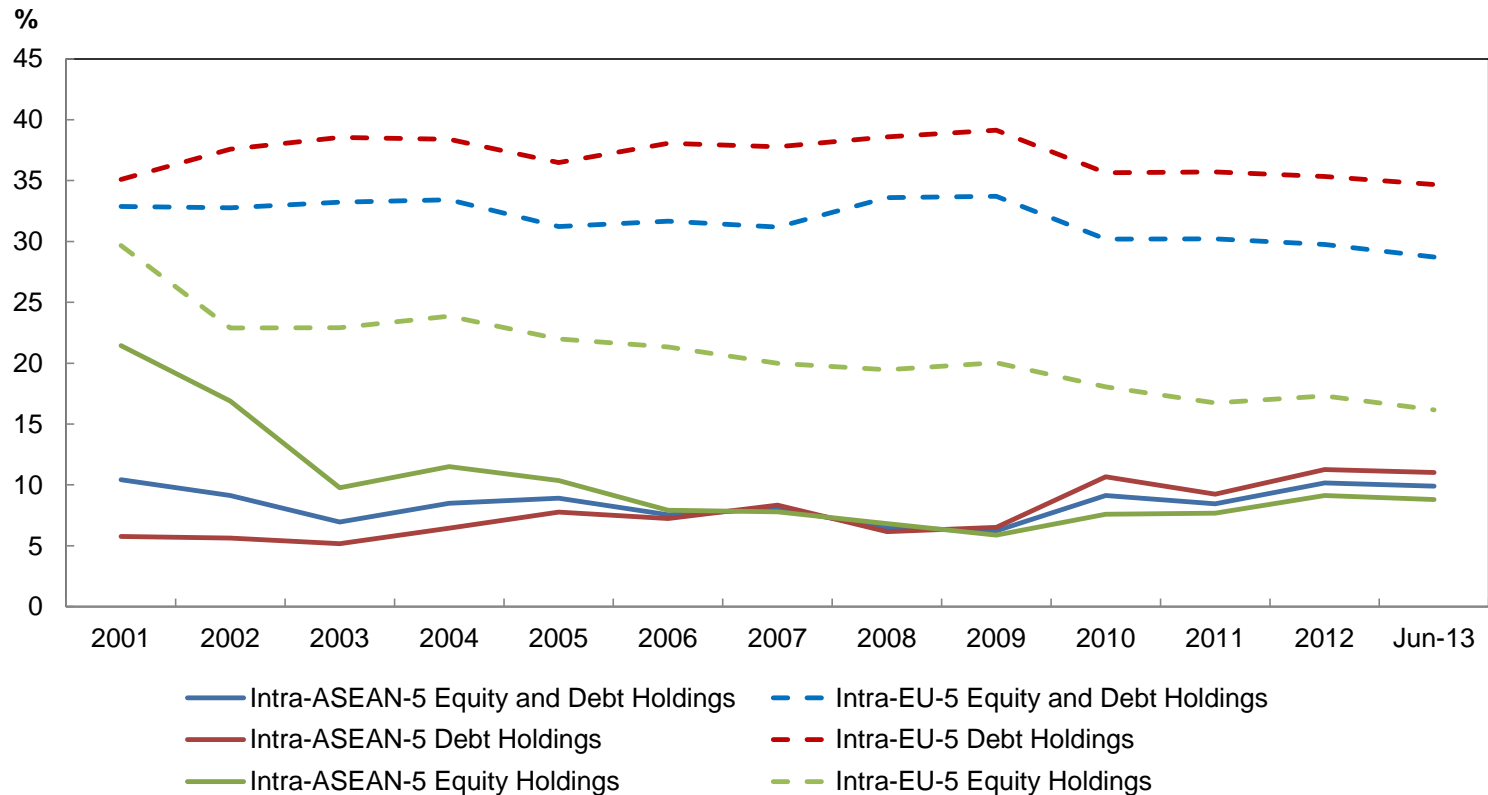
- Asian Bond Market Forum (ABMF) was established in 2010 to foster standardization of market practices and harmonization of regulations relating to cross-border bond transactions in the region.
- ASEAN+3 Multi-currency Bond Issuance Framework (AMBIF), a common regional bond issuance program, to allow qualified issuers from any country in ASEAN+3 to issue local currency bonds in any ASEAN+3 currency in the ASEAN+3 region. ABMF is also working to towards streamlining bond transaction flows including more simplified disclosure requirements.
- Also working to improve the regional cross-border settlement infrastructure through ASEAN+3 Cross-Border Settlement Infrastructure Forum.

Cross-border holdings of bonds have increased

- Traditionally, Asian investors have preferred to invest in their own home markets or in developed markets.
- But, we have seen intraregional holdings of debt securities continued rising.
- Intra-ASEAN5 bond holdings rose from 5.8% in 2001 to 11.0% in 2012.
- However, intra-regional holdings of equity is lower than bond at 8.8% in 2012 falling from more than 21% in 2001.

Intra-ASEAN5 holdings of bonds now higher than equity holdings

Intra-Regional Equity and Debt Holdings



European Financial Integration

- Single market for banks as part of the common market internal market.
- While there is common European rules, supervision remains mostly in national hands.
- Facilitated by the introduction of euro.
- Europe is currently working towards a banking union with Single Supervisory Mechanism and Single Resolution Mechanism.

EU vs ASEAN



2013

GDP Growth	0.11%
GDP(Mn USD)	14,647,977
Total Population	506,739,265



2013

GDP Growth	4.7%
GDP (Mn USD)	1,363,415
Total Population	615,676,470

European Commission vs ASEAN Secretariat



European Commission Headquarters in Brussels, Belgium

2012

Budget	\$4.3 billion
Number of employees	33,000



ASEAN Secretariat in Jakarta, Indonesia

2012

Budget	\$16 million
Number of employees	300

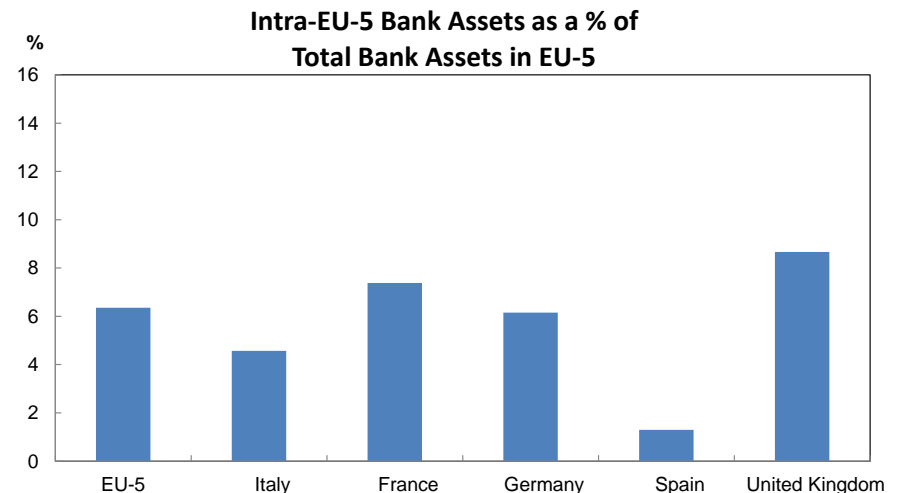
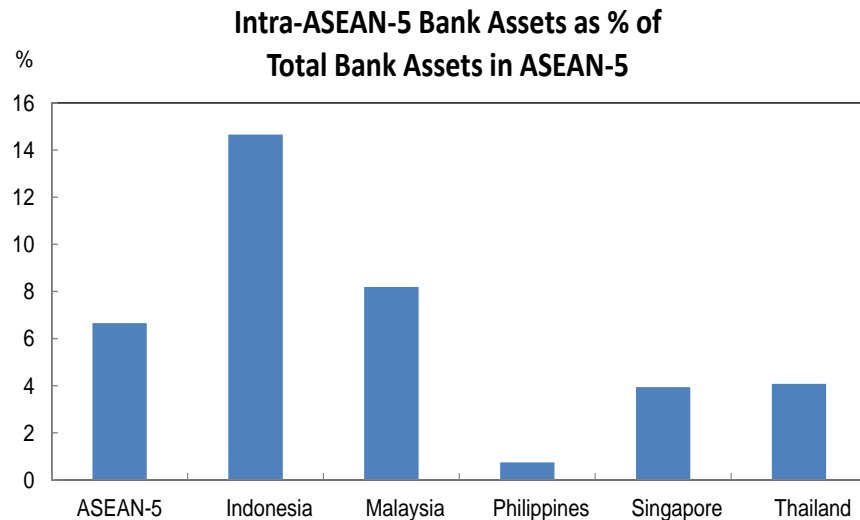
Benefits and Costs of Financial Integration

- Benefits
 - Increased risk sharing through portfolio diversification.
 - Entry of regional banks can ensure funds are channeled towards the most efficient use.
- Costs
 - Contagion risk and Spillover effects.
 - Increased risk taking and excessive leverage.

Experience of European Financial Integration

- Monetary union led to structural divergence.
- Core had 8% trade surplus while periphery had 8% trade deficit.
- Financial integration was incomplete
- The interbank market became rapidly highly integrated but retail banking remained largely fragmented along national lines.
- But during crisis, interbank lending dried up.

Intra-ASEAN-5 Bank Assets is at 6.7% of Total Banking Assets in ASEAN-5



Note: Data as of end-2012.

Source: Bank Indonesia, Bank Negara Malaysia, Bangko Sentral ng Pilipinas, Bankscope, and financial statements of respective banks.

Lessons for Asia

- Take a long term view and step by step approach. Ensure each stages are completed before taking the next one.
- Currency union much more demanding
- Proper bank regulation and supervision needed to ensure financial stability. Greater cross-border cooperation also essential.
- Strong domestic fiscal conditions and external balance are important for financial stability.
- Regional financial safety net can help during periods of liquidity crisis.

Conclusions

- Efforts to promote cross border trade in financial assets have been intensifying in ASEAN.
- Work is progressing to facilitate entries of regional banks into other ASEAN banking markets
- Local currency bond markets have flourished and there has been increasing intra-regional holdings of bonds.
- European experience suggests that financial integration is a long process and careful step by step approach is needed.
- Greater regional cooperation is needed to minimize the risks from integration.

Thank you

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