

Competition and Integration - Financial Centers and Financial Market Integration in Asia

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Outline

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2. How integrated are Asia's Financial Markets?
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Background: Mega-Trends in Asia

- Strong economic growth
- High saving and wealth accumulation
- Emergence of China and India
- Trade openness and integration
- Financial liberalization, innovation and globalization

How integrated are Asia's financial markets?

- Progress of financial integration through financial liberalization and capital account liberalization
- Weak evidence of increased financial integration based on 3 types measures- price measures, quantity measures and regulatory or institutional measures
- East Asia is relatively more linked to the global markets than integrated with one another in the region: the share of intra-region East Asian asset holdings is still low (8.6% in 2003)

Why Is Regional Financial Integration Weak?

- Low incentives for portfolio diversification within Asia
- Low degree of development and deregulation of financial markets
- Instability in monetary and exchange rate regimes
- Dominance of global “foreign” players

Needs for Financial Integration (regional or global)

- Low capital cost (esp., long-term investment)
- Efficient financial resource allocation
- Development of domestic financial infrastructure
- Risk diversification
- Consumption smoothing

Needs for Regional Financial Integration in Asia

- Avoid double mismatch that exacerbated 1997 Asian Financial Crisis
- Re-channel Asian savings into Asian economies
- Reduce the stock of international reserves
- Contribute to regional financial stability
- Promote intra-region trade and monetary integration

Progress of Regional Financial Cooperation

- Multiple fora – both public and private
- ASEAN, ASEAN +3, EMEAP
- Asian Bond Markets Initiative (ABMI)
- Asian Bond Fund I, II
- Chiang Mai Initiative

The Role of Financial Centers in Financial Development and Integration

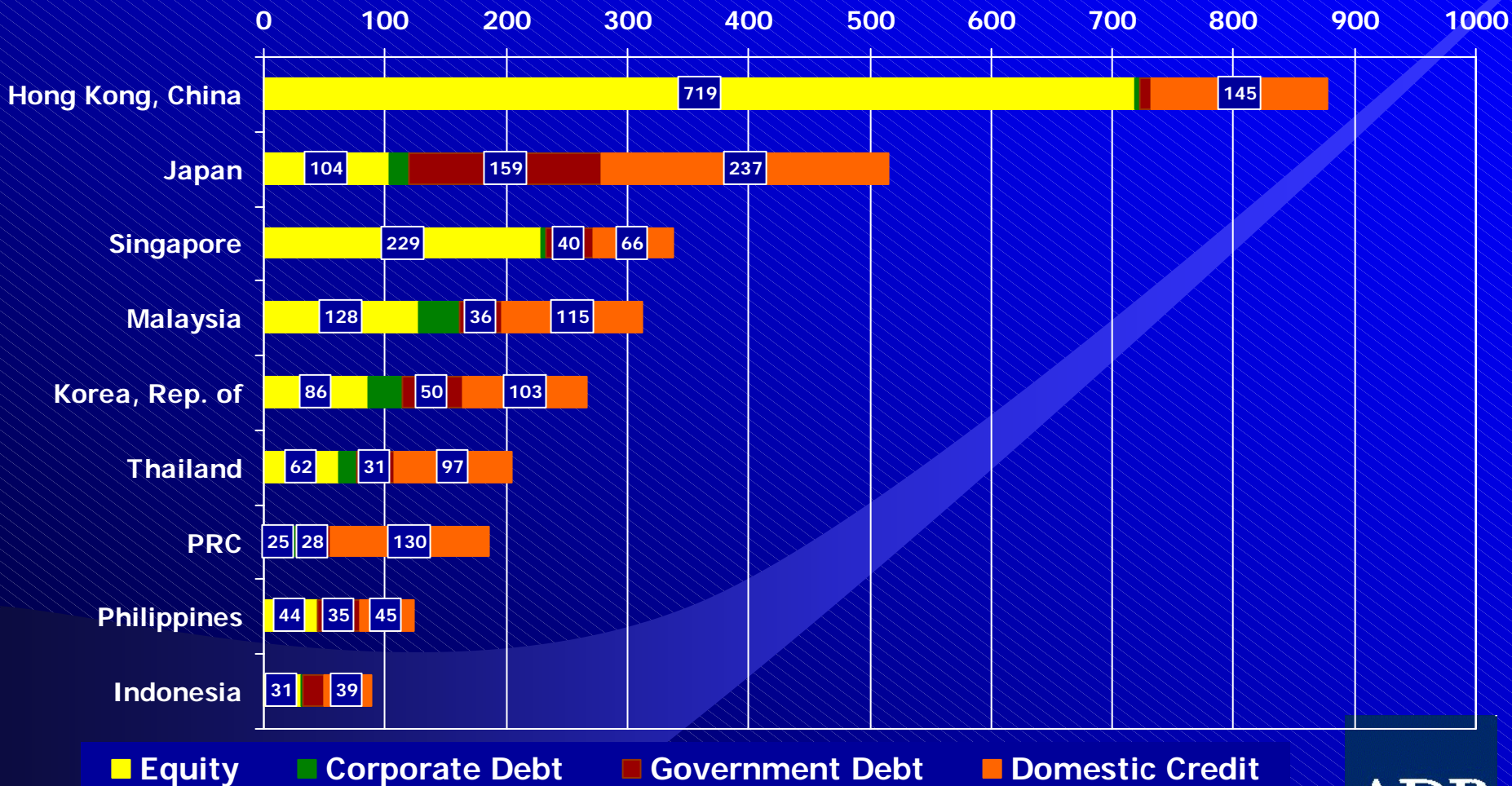
- Contribute to efficient and liquid financial markets in the region
- Support the fastest-growing Asian economies
- Scale economy and spillover effects
- Competition contributes to domestic financial market development and specialization in comparative advantage

Issues and Challenges for Asian Financial Centers

- Excessive competition– inefficiency and over-deregulation
- Risk of copy-cats: How to specialize?
- Dominance of global IFCs
- Domestic reform agenda: Diversifying the financial sector, improving human resources and regulatory framework
- Diverse exchange rate regimes and slow progress of monetary integration

Financial Assets (% of GDP)

As of September 2006



Source: AsianBondsOnline.

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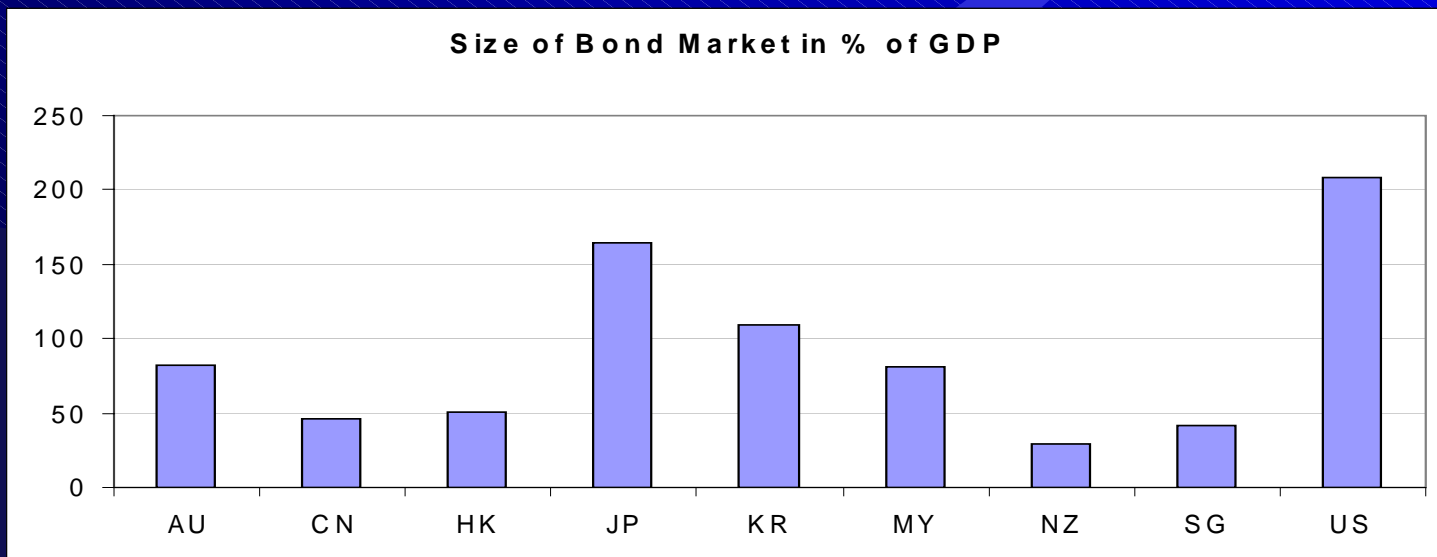
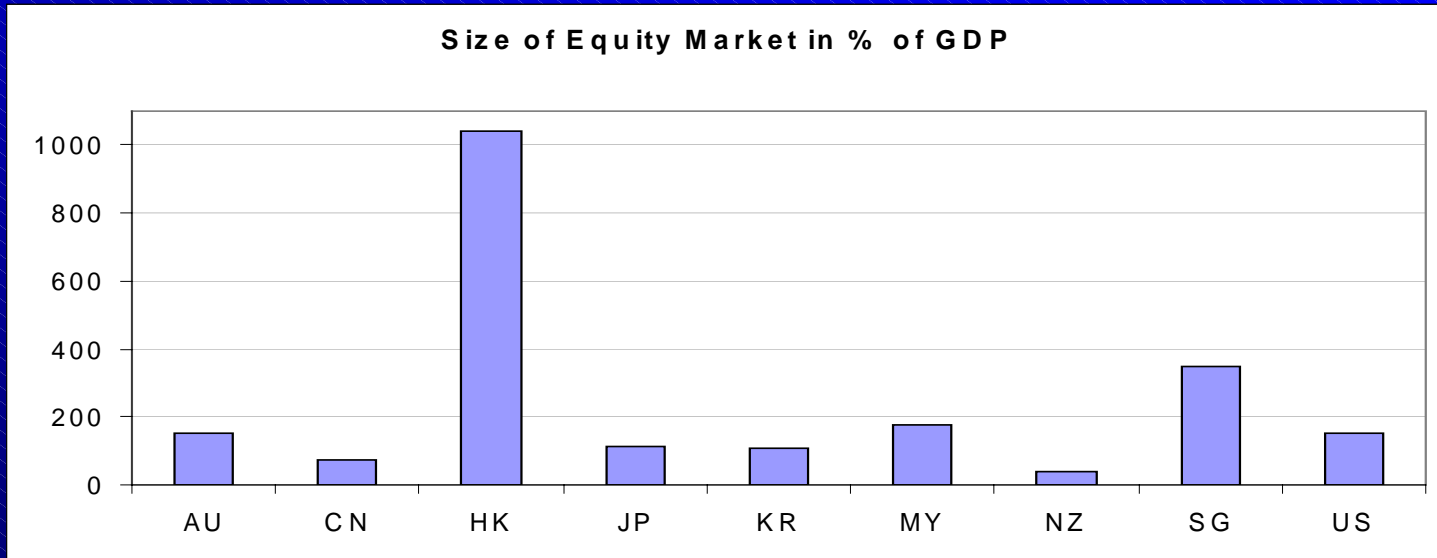
Bond and Equity markets

(June 2007, USD bn)

	Bonds	Equity	GDP
Australia	729.91	1,355.56	888.1
China, People's Rep. of	1,368.41	2,183.48	2,971.1
Hong Kong, China	99.20	2,028.00	194.9
Japan	6,843.13	4,681.05	4,163.4
Korea, Rep. of	1,035.84	1,042.16	943.9
Malaysia	139.13	306.96	172.5
New Zealand	37.53	51.99	128.8
Singapore	60.90	505.59	144.7
United States	28,725.40	20,785.76	13,768.8

Source: AsianBondsOnline.

Bond and Equity Market Size (June 2007, percent in GDP)



Cross-border Financial Activity, 2003

Economies	Net exports of financial services to GDP ratio (%)	Portfolio assets to GDP ratio (%)*	International Investment Position Asset (millions US\$)
Australia	0.052	25.30	380,848
Hong Kong, China	1.860	215.90	1,185,407
Japan	0.030	40.09	3,599,804
Korea	0.098	2.85	256,643
New Zealand	-0.034	27.00	53,274
Singapore	1.481	155.76	450,587
United Kingdom	0.900	95.78	6,394,917
United States	0.135	28.57	7,863,967

Source: A. Zarome 2007. "Concept of Offshore Financial Centers: In Search of an Operational Definition".
IMF Working Paper, Tables 8.

Global Financial Centers Index (GFCI): Ranks and Ratings of Selected Financial Centers

Financial Center	GFCI Rank	GFCI Rating
London	1	806
New York	2	787
Hong Kong	3	697
Singapore	4	673
Sydney	9	636
Tokyo	10	625
Melbourne	19	588
Dubai	22	575
Beijing	39	482
Mumbai	41	470
Seoul	42	464
Wellington	46	447

Source: M. Yeandle, M. Mainelli and I. Harris , 2007. "The Global Financial Centers Index 2". City of London. Table 2., p. 11. September 2007.

Key Messages

- Asia continues to emerge not just as a global trade and economic power but as a global financial player
- Asia's large and dynamic financial centers will contribute to financial market development and financial integration
- Diversifying financial sectors and Improvement of workforce and regulatory framework are a priority for success of financial centers in Asia
- Competition, together with cooperation and integration, produces a positive-sum game
- Region needs to work more for a stable, efficient and fully-integrated regional financial community