

# AEC BLUEPRINT 2025 ANALYSIS

# LIBERALISATION OF THE FINANCIAL SECTOR

## Foreword

The following report is part of a series, which attempts to provide a detailed analysis on the ASEAN Economic Community (AEC) Blueprint 2025. Each report will cover a single element of the blueprint, providing a comprehensive look at past achievements, present problems, and the future plans of the AEC. Special attention will be placed upon the strategic measures outlined in the AEC Blueprint 2025. This report aims to provide insight into the viability surrounding regional economic integration under the AEC.

## A. Past Plans

What were the targets in the AEC 2015 Blueprint?

ASEAN financial integration envisages a well integrated and smoothly functioning regional financial system with more liberalised capital account regimes and interlinked capital markets that will facilitate greater trade and investment flows in the region. This will be achieved through:

- (a) **Financial services liberalisation**
- (b) **Capital account liberalisation**
- (c) **Harmonisation of payments and settlements systems**

ASEAN aims to only achieve semi-integration in the financial sector by 2020. Full integration comparable to the level achieved by the core member countries of the European Union (EU) is deemed to be too ambitious in the next decade. ("Regional Cooperation in Finance", 2016)

### 1. Roadmap for Monetary and Financial Integration of ASEAN (RIA-Fin)

Endorsed in 2003, the RIA-Fin articulated ASEAN's goals and efforts within a roadmap format. The roadmap also affirmed the usage of a positive list modality, which meant that any commitments made would apply only to an explicit list of sectors. The task of integrating ASEAN's financial sector was divided into four separate areas:

- a. **Financial services liberalisation:** Intended to achieve free flow of financial services by 2015 through progressive removal of restrictions on financial services providers with the presence of Qualified ASEAN Banks (QABs) in other ASEAN countries.
- b. **Capital market development:** Intended to build capacity and lay the long-term infrastructure for development of ASEAN capital markets, with a long-term goal of achieving cross-border collaboration between the various capital markets in ASEAN. This is through enhancing market access, linkages and liquidity through such proposed initiatives as ASEAN Exchanges linkages, Bond Markets linkages; and promoting credit ratings comparability between domestic and international credit rating agencies.
- c. **Capital account liberalisation:** Intended to achieve freer flow of capital by 2015. This refers to the easing of capital restrictions and implementation of safeguards against volatility and systematic risks. In essence red tape surrounding Foreign Direct Investments (FDI), investment into equities, and bank borrowing will be addressed.
- d. **Currency Cooperation**  
To explore currency arrangements between member states aimed at facilitating intra-regional trade, investment and economic integration are viewed as part of ASEAN's goals in integrating financial markets. ("Regional Cooperation in Finance", 2016)

## 2. **AEC Blueprint 2015**

Put into effect in 2007, the AEC Blueprint 2015 focused on further clarifying the objectives of financial integration. Under the blueprint, the “ASEAN minus x” approach was adopted allowing for flexible commitments. The blueprint also adopted a schedule for financial services subsectors identified for liberalisation by 2015.

## 3. In 2008, the ASEAN Capital Markets Forum (ACMF) outlined six strategic components of the Implementation Plan:

### **A. Creating an Enabling Environment for Regional Integration**

1. Design and Implement a Mutual Recognition/Harmonization framework of gradually expanding scope and country coverage (Strategic Component I)

### **B. Creating the Market Infrastructure and Regionally Focused Products and Intermediaries**

1. Implement an Exchange Alliance framework to facilitate cross-border trades with local brokers initially; and strengthen and harmonize exchange governance, listing rules and corporate governance framework (Strategic Component II)
2. Promote new products and regionally active intermediaries to build awareness of ASEAN as an asset class (Strategic Component III)
3. Reinforce and expedite implementation of ongoing strategies and initiatives to strengthen and integrate bond markets. (Strategic Component IV)

### **C. Strengthening the Implementation Processes**

1. Refine the strategies for domestic capital market development in each ASEAN country and incorporate measures and milestones that support regional integration initiatives. (Strategic Component V)
2. Strengthen the ASEAN level working mechanisms in order to better coordinate regional integration initiatives and monitor and support its implementation at the country level. (Strategic Component VI)

## 4. **ASEAN Financial Integration Framework (AFIF)**

Adopted in 2011, the AFIF continued the blueprint’s initial objectives whilst committing ASEAN to the goal of a semi-integrated financial region by 2020. Several developments were added in subsequent installments:

- a. Differentiated timelines and targets for the ASEAN 5 and BCLMV nations in recognition of differing states of development and readiness
- b. Accord of equal access, treatment and environment to QABs;
- c. Regard to safeguard financial and monetary stability in the process of financial services liberalisation, capital market development, capital account liberalisation and harmonisation of payments and settlement systems; and
- d. Shared responsibility among AMS for enhanced collaboration on financial stability and capacity building.

## 5. **ASEAN Banking Integration Framework (ABIF)**

A framework agreement which was signed in 2015, the ABIF provided a guiding platform for the formation of bilateral agreements between member states concerning the banking industry. Under the framework, Qualified ASEAN Banks (QABs), which are defined by the individual bilateral agreements, will be given access to the markets of member states with the support of central banks.

## 6. **ASEAN Insurance Integration Framework (AIIF)**

AIIF was finalised and agreed upon to guide the progressive liberalization to ensure more competitive insurance markets and greater choice for consumers. Competitive insurance markets will lower the cost of insuring business risks, which will stimulate economic growth and spur intra-ASEAN trade. ASEAN members have agreed to prioritise the liberalisation of cross-border supply of Marine, Aviation and Goods in International Transit (MAT) insurance.

## **B. Past Achievements**

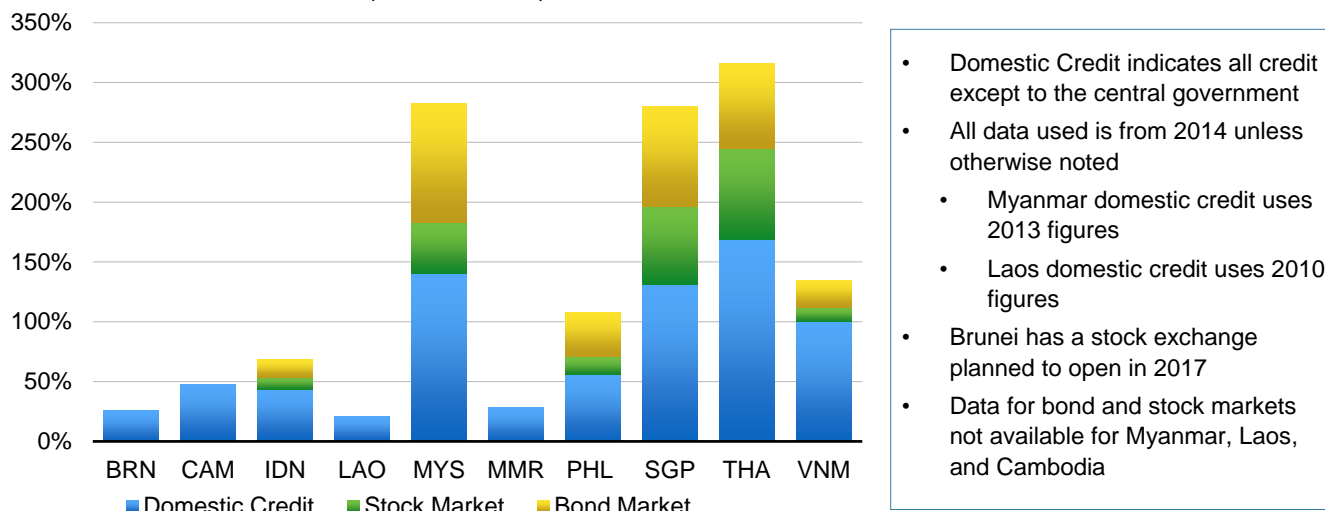
What has been achieved?

### 1. **State of ASEAN Capital markets**

As illustrated by the Figure #1, the disparity in the size of financial institutions and markets in member states shows a developmental gap between the ASEAN 5 and CLMV nations

- With exception to Singapore, the capital markets of member states offer limited depth and liquidity, and are therefore subject to excessive global capital flow volatility; this is only true when compared to the relatively more systematically insulated nature of developed capital markets around the world (Almekinders et al, 2014)
- Despite its size, ASEAN's market capitalisation jumped 12.2% in 2014 alone, whereas the Compounded Annual Growth Rate (CAGR) of the ASEAN 5 bond market for the past decade stood at 11.3% (ADB, 2015)
- Increased growth however, cannot be attributed to financial integration between member states

Figure #1: ASEAN Capital Market Depth  
(In % of GDP)



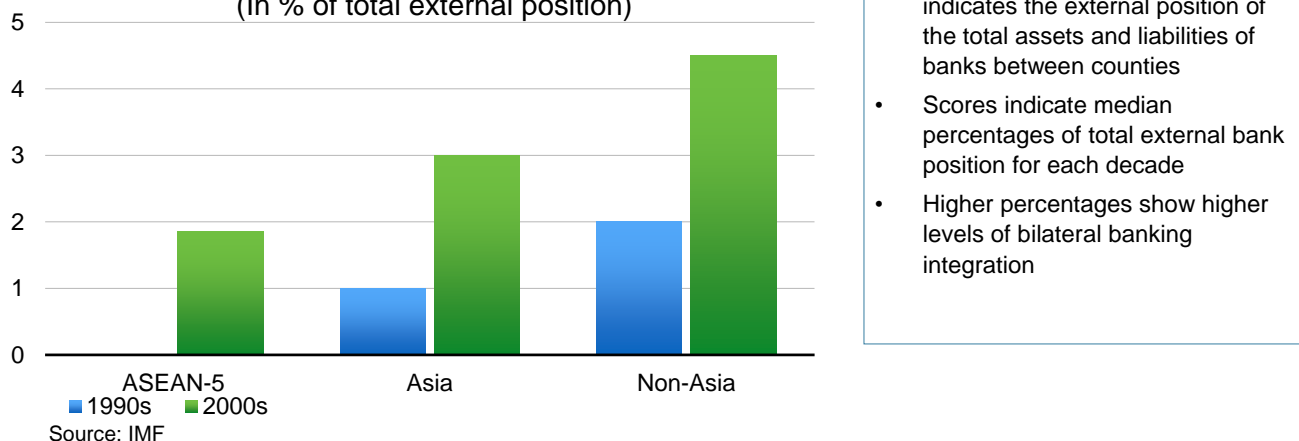
Source: World Bank, ADB

## 2. Financial Services Liberalisation

As key financial intermediaries for the region, banks make up the bulk of ASEAN's financial markets and can be used as indicators of financial services integration through cross border activities.

- As demonstrated in Figure #2, bilateral banking integration is relatively low within member states when compared to the region and the rest of the world.
- In 2009, foreign banks made up 18% of total commercial banks in Malaysia, the Philippines, and Thailand; Malaysia accounted for the highest share of foreign ASEAN based banks at 8.5%. (IMF, 2015) Foreign banks in AMS countries are largely big sized international banks as opposed to ASEAN-based banks. (ADB, 2013)
- Except Maybank Banking Berhad, no home grown ASEAN based bank has a branch or subsidiary in all ASEAN countries; on the other hand, foreign owned and controlled insurance companies are pervasive amongst member states, especially amongst the lesser-developed markets. (Lee, 2015)
- The ABIF which was signed into effect by the Sixth Package of the AFAS in large part hopes to solve the lack of ASEAN banking integration (Indonesian Ministry of Finance, 2015)

Figure #2: Bilateral Banking Integration  
(In % of total external position)



### 3. Capital Account Liberalisation

- The preliminary assessment and identification of rules relating to foreign exchange transactions has been completed.
- Member states have drafted individual roadmaps to liberalise capital account regimes.

### 4. Capital Market Development

- a. **Agreement to adopt ISO20022** as a common standard for fund transfers in ASEAN, upon readiness of individual countries
- b. **ASEAN Trading Link** electronically connects exchanges in Malaysia, Singapore and Thailand providing investors with easier and more seamless access into ASEAN markets from one single access point.
- c. **ASEAN Disclosure Standards** provides significant efficiencies to issuers as they need only to adopt a single set of disclosure standards for prospectuses in an offering across multiple ASEAN jurisdictions. Malaysia, Thailand and Singapore are signatories to the Scheme. The Scheme is benchmarked against the International **Organisation of Securities Commissions' ("IOSCO")** disclosure standards. A Memorandum of Understanding (MoU) which establishes a **Streamlined Review Framework** for the ASEAN Common Prospectus.
- d. Through the **Memorandum of Understanding (MoU) on Expedited Entry of Secondary Listings** among regulators and exchanges from Malaysia, Singapore and Thailand, the time-to-market for corporations seeking a secondary listing in a participating ASEAN country has been reduced from the normal timeframe of up to 16 weeks to 35 business days.
- e. The **ASEAN Corporate Governance Scorecard** is based on a corporate governance ranking methodology which leverages on methodologies already implemented in ASEAN countries, as well as those applied by multilateral agencies such as the OECD. The Scorecard aims to raise corporate governance standards and practices, showcase and enhance the visibility of well-governed PLCs and promote ASEAN as an asset class internationally.
- f. The **ASEAN Capital Markets Infrastructure Blueprint** aims to enhance connectivity of ASEAN capital markets through post trading linkages. Having greater access to different markets helps ASEAN investors to diversify risks and issuers to lower borrowing costs, while keeping transactions efficient.
- g. The **ASEAN Bond Market Development Scorecard** monitors development of bond market development. Starting with Malaysia, Singapore and Thailand, ASEAN member states have also developed and adopted the **ASEAN Debt Securities Standards**.
- h. ASEAN members monitor the progress of capital account liberalisation through the **ASEAN Capital Account Liberalisation Heat map** and **Individual Milestones Blueprint**.
- i. The **Policy Dialogue Process on Capital Flows and Safeguard Mechanisms for Capital Account Liberalisation** allow ASEAN members to monitor capital flow trends and exchange experiences on capital flow management.
- j. The **Principles and Guidelines on Pre-Departure Orientation Program** ensure that migrant workers receive adequate information to prepare them for their new life in their new destination, supporting a large group in ASEAN that may lack access to financial education.
- k. A **Collective Investment Scheme (CIS)** was operationalised in 2014, allowing for the cross border offering of products to signatory countries; five companies have already had their products approved as of 2015.

## C. Present Challenges

What are the current issues?

### 1. Developmental Gap

The developmental gap which exists between ASEAN financial markets defines and divides the monetary and fiscal policy goals of each member state. This in turn means that integration efforts are often retarded by national restrictions and regulations, which is exacerbated by the ASEAN minus x formula.

### 2. Public-Private Collaboration

The success of ASEAN financial sector integration hinges not only on the policy reform of governments, but also the efforts of private sector financial institutions and agents. Whilst policy reform has seen progress, greater efforts will need to be placed on public private sector collaboration in order to see the true benefits of integration efforts. In particular, a lack of private sector consultations has been highlighted as a key problem with current policy direction. (Chia, 2011)

### 3. Translating regional commitments to country policy

Although the broad objectives and overarching regional commitments have been developed, comprehensive initiatives have been lacking. As ASEAN continues to remain sensitive towards the policy objectives of member states, various exclusions and exceptions and a time consuming national legislative process have been marked as detrimental to financial integration. (Chia, 2011)

## D. Future Plans

What new measures are included in the AEC 2025 Blueprint?

The AEC Blueprint 2025 refocuses financial sector integration with new measures relating to financial inclusion and stability; these two new areas largely involve information sharing initiatives and the adoption of best practices with regards to policy.

## E. AEC 2025 Blueprint Analysis

What do the measures entail?

Strategic Measure	Analysis
<b>1 Strengthen Financial Integration</b>	
<ul style="list-style-type: none"> <li>Commit to ATISA as a platform to link regional financial markets and dialogue partners</li> </ul>	<ul style="list-style-type: none"> <li>According to Senior Level Committee declaration on ASEAN Financial Integration, ATISA will focus incorporating elements present within the ASEAN Plus FTAs into a legal framework to further financial sector liberalisation.</li> <li>A date for deliberations concerning ATISA and the drafting of preliminary objectives and negotiations has yet to be set</li> <li>As the completion of the final rounds of the AFAS are now projected to stretch into 2017, ATISA will likely take a back seat in the short term future</li> </ul>
<ul style="list-style-type: none"> <li>Follow through on the ABIF, providing greater market access and operational flexibility for QABs</li> </ul>	<ul style="list-style-type: none"> <li>According to the ABIF timeline of implementation:               <ul style="list-style-type: none"> <li>ASEAN 5 nations are to have agreements with at least one other member state by 2018;</li> <li>Whereas all member states are to have agreements with at least one other member state by 2020</li> </ul> </li> <li>Following the completion of bilateral agreement targets, the ABIF stipulates a multilateral stage which will establish ASEAN-wide guidelines. These guidelines will allow banks founded within member states to offer their services within other ASEAN nations. (Shimizu, 2014)</li> </ul>
<ul style="list-style-type: none"> <li>Use the AIIF to ensure greater risk diversification, underwriting capacity, sector supervision, and regulatory frameworks</li> </ul>	<ul style="list-style-type: none"> <li>With the MAT sectors addressed, the AIIF may seek to address the catastrophe insurance and reinsurance markets</li> <li>Whilst foreign ownership laws in the insurance industry are largely liberal, the cross border trade of insurance products remains widely restricted. (Abbas, 2013) (Adams et al, 2015)</li> <li>It is likely the AIIF will be further amended and developed to address issues of cross border trade.</li> <li>The ASEAN Insurance Council (AIC) has announced plans to execute a two-year master plan targeting 7% growth across insurance markets, this would involve a strategic quality control framework likely to tie into the AIIF. (AIC, 2016)</li> </ul>
<ul style="list-style-type: none"> <li>Clear settlement and custody linkages to facilitate regional investment</li> <li>Actualise ASEAN Capital Market Infrastructure (ACMI) Blueprint objectives</li> </ul>	<ul style="list-style-type: none"> <li>The Working Committee on Payment and Settlement Systems (WC-PSS) is assessing the current situation and making policy recommendations concerning settlement systems.</li> <li>ASEAN+3 countries are working to create a settlement system to support cross-border bond transactions under the Asian Bond Market Initiative (ABMI)</li> <li>Recent progress includes the completion of a reassessment of business feasibility relating to the establishment of a regional settlement intermediary (RSI) by Task Force 4</li> <li>The Cross Border Settlement infrastructure Forum working in collaboration with the ASEAN+3 Bond Market Forum (ABMF) has suggested that ASEAN adopt a Central Securities Depository - Real Time Gross Settlement System (CSD-RTGS). Put simply, a system run by central banks which allows securities to be transferred between individuals. (Shimizu, 2014)</li> </ul>

- Develop sovereign and corporate bond markets
- Currently, the ASEAN focus for bond markets would be the facilitation of cross border transactions and information availability; studying commonalities and difference in bond insurance documentation and procedures has been recognised as a viable first step for ASEAN as declared during the ASEAN+3 Finance Ministers Summit. (ASEAN, 2014)
- In the long term, ASEAN hopes to establish the ASEAN+3 Multi-Currency Bond Issuance Framework (AMBIF) which will act as a common regional bond issuance program for professional investors.

## 2 Promote Financial Inclusion

- Enhance financing ecosystem for MSMEs
- Establish credit bureaus/other facilities or mechanisms for MSMEs
- Currently, access to financing for MSMEs is hampered by a variety of factors. These include stringent collateral requirements, inadequate creditor rights, a lack of a central bureau for credit information for smaller financing markets, and a lack of legal policies promoting alternative financing. (ERIA, 2014)
- It is likely that ASEAN will attempt to create a guiding framework so as to instill best practices in the region. Furthermore, the facilitation of cross-border financing for MSMEs could be executed through liberalising credit policies.
- Whilst unlikely, a regional credit bureau for MSMEs could be created.
- Expand scope of financial access and literacy
- Focus on financial infrastructure
- Develop best practices
- Information and technology sharing would be necessary to successfully expand the scope of financial access and develop financial infrastructure.
- Financial literacy would involve reforming consumer protection laws across the region that will likely involve the adoption of best international practices into policy.
- Furthermore, public awareness campaigns and educational programs would raise financial literacy in the region.

## 3 Ensure Financial Stability

- Intensify macroeconomic and financial surveillance
- Identify system risks
- Exchange macroeconomic information
- ASEAN has taken an information sharing approach on macro prudential policies and capital flow management measures in order to advance regional surveillance.
- Furthermore, the ASEAN+3 and the Regional Comprehensive Economic Partnership (RCEP) have both expanded the scope of integration to include surveillance prerogatives.
- The ASEAN Integration Monitoring Office (AIMO), Chiang Mai Initiative Multilateralization (CMIM), and independent ASEAN+3 Macroeconomic Research Office (AMRO), will most likely be further enhanced so as to improve regional surveillance.
- Implement safeguards within regional banking agreements
- As stated above, the RCEP will likely include safeguards.
- Furthermore the bilateral agreements finalised under the ABIF will likely have an emphasis on regional safeguards; the multilateral stage of the ABIF will further this concept.
- Emphasise cohesive prudential regulations
- Follow international best practices/regulatory standards
- As stated, this measure entails that ASEAN member states will seek to strengthen their bank resolution frameworks by adopting the best international practice and Financial Stability Board (FSB) initiatives.

## 4 Focus on Cross-Cutting Areas

- Ensure capital account liberalisation does not interfere with national agendas
  - Safeguards against systemic risk from liberalisation need to be allowed
  - Monitor progress of capital account liberalisation
  - This will likely involve delineating national agenda concerns and systemic risk safeguards with regards to capital account liberalisation. Doing so will allow for the successful establishment of baseline commitments in capital account liberalisation.
  - A scorecard will probably be developed to measure progress in capital account liberalisation.
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- Enhance payment and settlement systems through standardising settlement infrastructure
  - Harmonise regulatory standards according to best practices
  - As discussed in the previous section about settlement systems, a preliminary study has been initiated.
  - If the ABMF's advice is heeded, a CSD-RTGS will help to harmonise the region's settlement systems.
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- Capacity building to narrow financial development gap through information sharing
  - This measure further emphasises the need for information sharing and learning programmes across ASEAN with regards to financial literacy, best practices, and macroeconomic policy.

## F. Conclusion

What does the AEC 2025 Blueprint mean in terms of the Financial Integration?

- Given the development gaps among ASEAN member states, ASEAN has set itself a conservative target for financial integration. Although the AEC Blueprint 2025 takes a step forward by introducing two new areas of focus, financial inclusion and stability, the majority of strategic measures offered do not hint towards any big changes in policy in achieving financial integration.
- No central body such as the European Central Bank has been proposed, which continues to confirm that the AEC's goals lie towards financial integration tempered by flexibility rather than clear-cut unified policy.
- Likely to be further developed under ATISA by 2017, the Blueprint focuses on completing previous objectives and established initiatives.

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