Time for capital markets in Asia to rise

Remarks by Mr. Thirachai Phuvanatnaranubala, Secretary-General, Securities and Exchange Commission, Thailand and Chairman of the ASEAN Capital Markets Forum
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Capital Markets in Asia are set to rise in prominence. This is caused by the global financial crisis. The crisis has turned future world economic development into a tale of two halves.

The half of the advanced markets is set to grow much more slowly, with the half of the emerging markets enjoying substantially faster growth. It will open up opportunities for Asian capital markets to take away some of the business and the role previously of the advanced markets.

The slow but calculated move to raise the international usage of the Chinese Yuan is a case in point. It will define the future of Hong Kong and whichever other centers that can serve such business well.

In the long run, it may even lead the Chinese Yuan to be the core currency around which other Asian currencies revolve. The more the Asian countries become parts of the same supply chain with China, the stronger the role of the Chinese Yuan.

You may recall that a few years ago Turkey expressed strong interest to join the Euro, but faced a delay. Recently there have been comments in the Turkish press suggesting a rethink. Would it not be better to join an Asian currency arrangement that may occur in the future instead of looking to Europe?

This is definitely an important key driver for more rapid capital market development in ASEAN. But there are also others. What are they?

First, the move towards ASEAN Economic Community will lead to more intra-regional trade in goods and services. A lot of financing will be required, and the financing has to expand beyond the banking channel into the capital market channel.

Second, we must encourage ASEAN to invest more into each other. In the past model, countries will invest surplus savings in the advanced markets only to be recycled back to countries with deficit. We must make ASEAN investors more comfortable with ASEAN financial products.

Third, the Asian Crisis had shown that capital markets can be much better than the banking channel in allocating scarce imported capital to deserving projects. Because bank lending is a secret only between the bank and its customer, it would easily lead to over investment and over capacity.

Capital markets, on the other hand, are transparent. Allocation of resources is based on comparative risk and return. It is also subjected to public analysis by stock brokers, financial advisors, financial press, credit rating agencies and many others. Not only do the investors know of your future business plan, but also your competitors. Over expansion will be stopped in its track.

Capital markets can help with risk management too. The existence of local currency bond markets lessens the risk of both the currency mismatch and the maturity mismatch.

But the most important key driver for capital market development is actually the need for a liquidity crisis tool.

In Thailand, the 1997 crisis started with the finance companies. Soon, Thai banks stopped lending to finance companies. After that, large Thai banks stopped lending to small Thai banks. Finally, foreign banks stopped lending to Thai banks. In the end, even industrial companies demanded cash before delivery.

In that situation, the Bank of Thailand had no way to act as the lender of last resort. Whatever liquidity it put in stayed only at the banks that had no need. The banks that had a need had run out of market instruments a long time ago.

The Bank of Thailand had no choice at that time but to lend money to the finance companies directly through the Financial Institutions Development Fund. They took in boxes of loan contracts. But it was only for visual comfort because the law required debtors' consent to legally transfer the loans, which was impossible to do at the height of the crisis.

A large part of the loans went bad, and the Bank of Thailand was badly criticized. The staff was publicly investigated and ridiculed. It is ironic that in the global financial crisis in 2008-9, all the big advance countries did exactly the same. All the central banks in Europe and the USA went in to rescue their banks. All were rescued except poor Lehman Brothers.

In hindsight, the criticism to the Bank of Thailand was harsh. A law has since been passed to prevent the Bank of Thailand from making such unsecured lending again. So what will happen when there is the next financial crisis?

Without the Financial Institutions Development Fund, the only way for banks in Thailand to look after themselves is to speed up on development of the bond markets. Banks must have more instruments on hand that they can always sell in the market regardless of their reputation.

For ASEAN capital market development agendas, there is no key driver as important as this one.
