

Asian Capital Market Law and Regulation Forum:  
Japan, China and Korea

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**How to create Common and Suitable Self-  
Regulatory Rules in Asian Capital Market?**  
**-- For the recognition of the common infrastructure --**

アジア域内共通資本市場の自主規制ルール構築の可能性

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1.

**Were Asia's High Savings  
the origin of the global  
financial crisis?**

# The Turner review-U.K. FSA

A regulatory response to the global banking crisis

March 2009, U.K.FSA's Lord Turner  
published Review

[http://www.fsa.gov.uk/pages/Library/Communication/Speeches/2009/0318\\_at.shtml](http://www.fsa.gov.uk/pages/Library/Communication/Speeches/2009/0318_at.shtml)

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# What -FSA believes- went wrong?

## Drivers of the crisis

**The development of the global system of securitized credit intermediation** was stimulated, by **large global macro imbalances** (世界的な経常収支のインバランス), by **very low real interest rates, the desperate search for yield uplift.**

It entailed rapid growth of risky lending and an explosion of financial innovation, the alphabet soup of structured credit and credit derivatives.

And it was characterized by **7 features** which first helped create the boom and are now making its aftermath so economically harmful.

# 7 features

- **Massive growth in the scale and complexity of securitized credit**, facilitated by inadequate capital requirements for trading activity. - Risky lending and an explosion of financial innovation, the alphabet soup of structured credit and credit derivatives.
- **Extensive commercial bank involvement** in trading activities, which meant that big trading book losses had consequences for confidence in the core banking system.
- Growth and increased **leverage** of the financial sector in several different forms, which **amplified both the upswing and the downswing we now face**.
- **Changing forms of maturity transformation** within the banking and ‘**(related offshore) shadow(SIV) banking**’ sectors, with increasing dependence on market funding = “**liquidity through marketability**”. (Northern Rockのケース)
- A misplaced reliance on sophisticated maths to manage the risks.
- **Hard-wired procyclicality (景気循環の増幅効果) in banks’ systems and processes**. Like rating-triggers, margin-calls or haircuts (レポ市場におけるイニシアル・マージンの慣行). Features such as excessive reliance on ratings – which hard-wired the system to be unstable, both on the way up and the way down.
- **Inadequate bank capital buffers**, leaving banks with an impaired ability to keep lending to the real economy when the downturn came.

# Global Macro Imbalance, Very Low Real Interest Rates

A **key driver** of those imbalances has been **very high savings rates** in countries like China; since **these high savings** exceed domestic investment, China and other countries **must accumulate claims on the rest of the world**.

But since, in addition, China and several other surplus countries are **committed to fixed or significantly managed exchange rates**, these rising claims take the form of **central bank reserves**.

These are typically invested not in a wide array of equity, property or fixed income assets – but almost exclusively in apparently risk-free or close to risk-free government bonds or government guaranteed bonds.

This in turn has **driven a reduction in real risk-free rates** of interest to historically low levels.

In 1990 an investor could invest in the UK or the US in risk-free index-linked government bonds at a yield to maturity of over 3% real; for the last five years the yield has been less than 2% and at times as low as 1%.

These very low medium- and long-term real interest rates have in turn driven **two effects**:

# Two Effects

- **Firstly**, they have **helped drive rapid growth of credit extension in some developed countries, particularly in the US and the UK** – and particularly but not exclusively for residential mortgages – with this growth accompanied by a degradation of credit standards, and fuelling property price booms which for a time made those lower credit standards appear costless.
- **Secondly**, they have **driven among investors a ferocious search for yield** – a desire among investors who wish to invest in bond-like instruments to gain **as much as possible spread above the risk-free rate**, to offset at least partially the declining risk-free rate. Twenty years ago a pension fund or insurance company selling annuities could invest at 3.5% real yield to maturity on an entirely risk-free basis; now it would be only 1.5%. So any products which appear to add 10, 20 or 30 basis points to that yield, without adding too much risk, have looked very attractive.



2.

How can Asia contribute to  
normalize the global macro  
imbalances?

## In order to do that ---

- An Asian Common and Suitable Capital Market, which would enable the **abundant savings in the region to be circulated within the region.**

3.  
Asian regional economy and  
trade

# Asian regional economy and trade

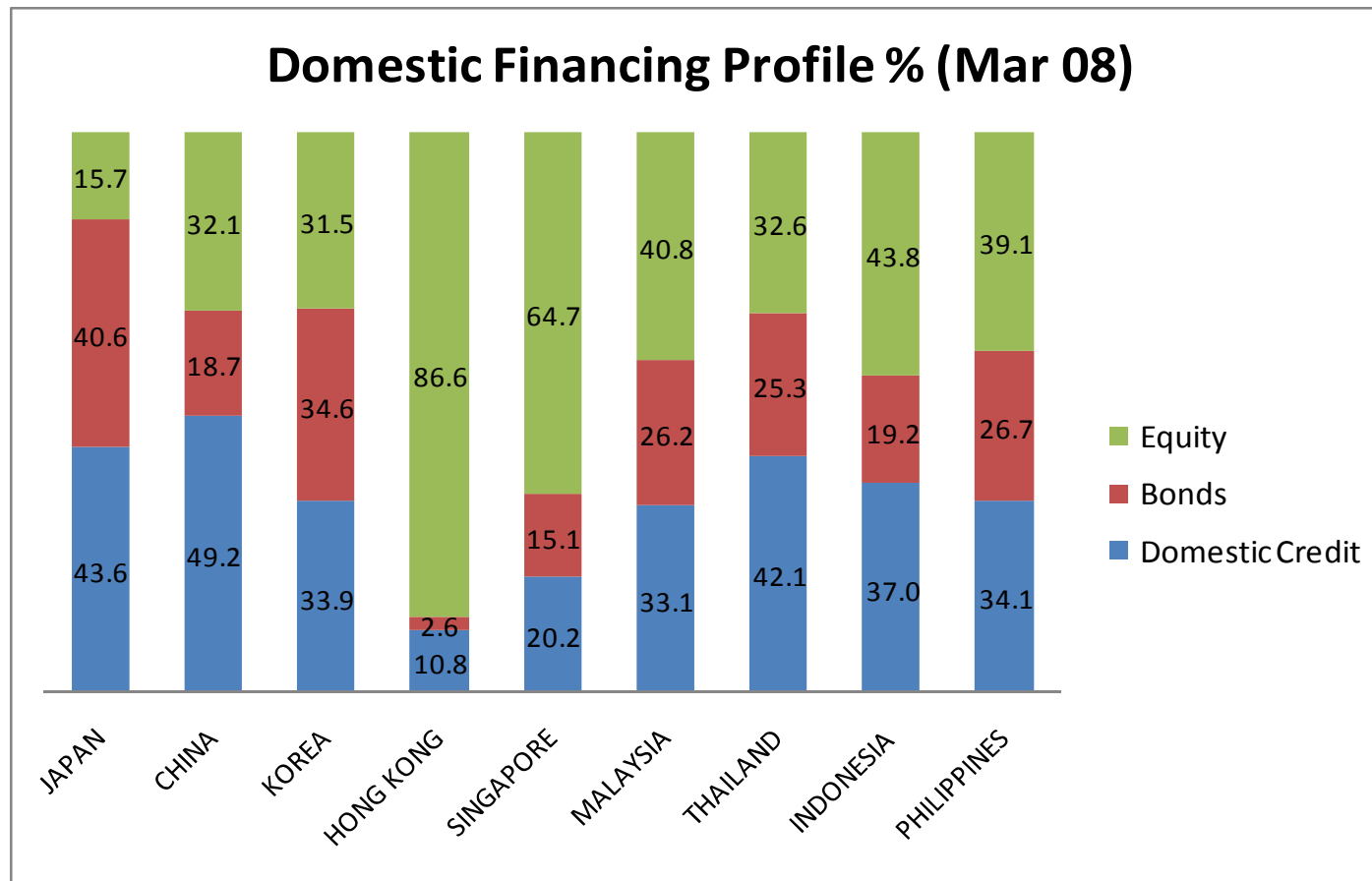
- Some Asian countries focus on their areas of comparative advantage, and specialize in producing intermediate goods
- A sophisticated division of labour structure has been formed across national borders in the region
- The result is superior and competitive “Made in Asia” products, e.g. electrical appliances and vehicles
- Deeper trade interdependency between Japan and other Asian countries

4.

## Features of Asian financial & capital markets

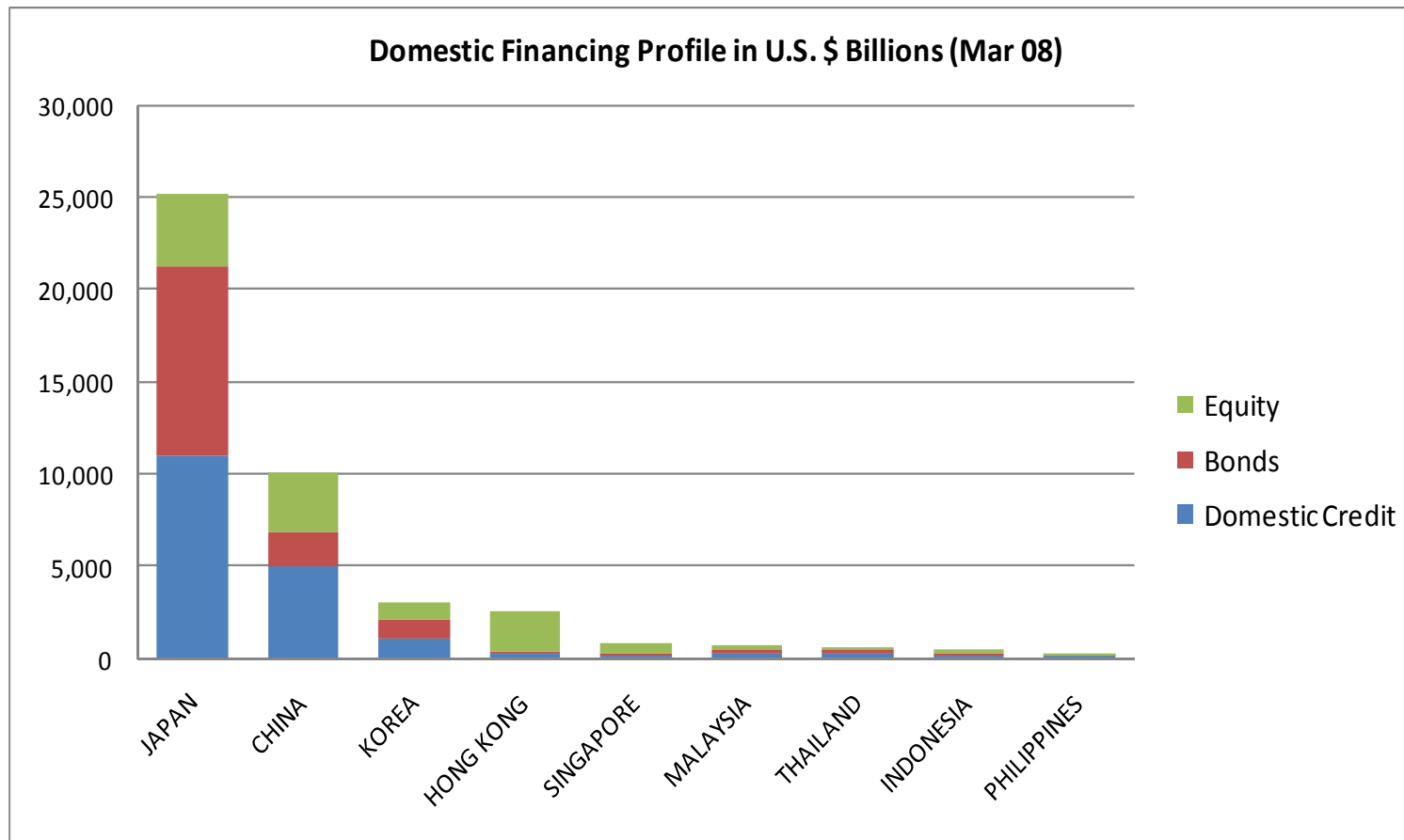
# Features of Asian financial & capital markets

Asian markets are achieving a good balance in their domestic financing profiles, despite the prevalence of bank-centered indirect financing systems in the region.



# The absence of common infrastructure

- Domestic markets evolving
- Cooperation and alignment between Japan, Korea and China is key
- **Common infrastructure needed to create common capital markets in Asia**



5.

For the creation of an integrated  
Asian Wholesale (Professional)  
Capital Market



# An Asian investment banker's perspective

- Huge Asian capital reserves provide an opportunity for Asian financial institutions to take the lead in capital markets in Asia
- Asian financial institutions are not leading the market in terms of capital disbursement and price making – European and US financial institutions still dominate in this area
- Why is it that Asian issuers need to raise capital in London or New York?
- Advanced Asian financial institutions have a responsibility to take the lead
- Why not integrate Asian capital markets to create a viable option in addition to London and New York?

# Importance of Common Infrastructure

- The absence of common infrastructure for the integrated Asian Wholesale (Professional) Capital Market.
- As an important element in an integrated Asian Wholesale (Professional) Capital Market , which would enable the abundant savings in the region to be circulated within the region, is yet to be developed.
- Suitable Self-Regulatory Rules for the market is essential.

# Integrated Markets?

- Need to recognize **diversity** in Asia
- Integration – what degree is required?
- Focus on common infrastructure, i.e. a cross-border wholesale (= professional) market accessible by Asian countries
- The concept of an integrated Asian Wholesale (Professional) Capital Market as a self-contained market, enabling savings accumulated in the region to circulate within the region

6.

What are CMAA / IPMA / IMCA?

# Purpose of Capital Markets Association for Asia (CMAA)

- **Formulate proposals for the self-governing rules and recommendations for issuing entities and other users of the Asian regional financial & capital markets**
- Coordinate opinions regarding legal systems and rules
- Foster dialogue with CMAA participants
- Conduct research, formulate proposals, increase awareness
- The ultimate purpose of the CMAA is to increase the reliability and convenience of all financial and capital markets in Asia and to establish appealing markets for all users

# About the CMAA

**Name:** Capital Markets Association for Asia (CMAA)

**Status of the Group:** A voluntary organization bringing together participants who agree with the purpose of establishment of the CMAA.

Basically, members join in an individual capacity, but corporate entities are not prevented from joining.

**Membership fee:** No membership fees

**Admission to the Association:** Admission of new members is decided by the Officials Meeting based on the recommendation of several existing members.

**Inauguration:** The inauguration of the CMAA was officially announced at the “General Meeting for the Establishment of the Capital Markets Association for Asia” held on June 19, 2007.

**Chairperson:** Nobuyuki Idei, CEO of Quantum Leaps Corporation, Ex. Sony CEO

**Secretary-General and Executive President:** Shigehito Inukai, Professor, Faculty of Law, Waseda University

# For the creation of the Asian version of the IPMA\* Handbook



ICMA kindly provided CMAA their self-regulatory handbook for further study. CMAA and Waseda University GCOE have been making the joint effort to create Waseda/CMAA Handbook for Asian Market Players.

\* IPMA was the main trade organization concerned with new issue procedure in the Euromarkets. IPMA's original core role was the harmonization and the establishment of accepted best practice in the primary markets.

# ICMA

- ICMA is the representative body and voice for all capital market constituencies with a European focus
- IPMA merged with the International Securities Market association (ISMA – the successor to the AIBD) in July 2005
- The merger created the International Capital Market Association (ICMA)
- ICMA is a trade association and a self-regulatory body for the secondary markets
- ICMA has opened up its membership beyond the banks and securities houses to now include institutional investors and borrowers
- ICMA is unique among financial industry associations in that it represents a broad range of capital market interests in almost 50 countries
- Its members now include global investment banks and smaller regional banks, as well as asset managers, exchanges, central banks, law firms and other professional advisors



# ICMA's Role

- Development and maintenance of high standards of market practice
- Fostering appropriate levels (and content) of regulation
- Provision of trade support and data systems and services
- Educating market participants and others through training and research
- Facilitating communication and establishing information forums

**Thank You!**

