

Strengthening of Financial Supervisory Structure in Asia

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I. Backgrounds

- Financial crisis caused by capital liberalization resulted the reform of financial supervisory system: Unified supervisory system
- In 1998, UK assigned the task of supervision of entire financial system to a single authority (FSA)
- Bank of England transferred the bank supervision to FSA
- Large number of countries like Japan and Korea followed UK system and established single agency of supervision

East Asian Financial Supervisory Systems

- Japan established FSA in 1998 (government body)
- Korea reformed financial supervisory system in 1998 just after the crisis.
(Established Financial Supervisory Service(FSS) as a governmental and independent body in 1999, and Financial Supervisory Commission(reformed as Financial Service Commission(FSC) in 2008) as a government body in 1998)
- China maintained 3 diversified supervisory agencies (People's Bank of China, Insurance Regulatory Commission of China, and Securities Regulatory Commission of China)

II. Lessons from Global Financial Crisis

- Unified financial supervision system fails to avoid the financial crisis : Strengthen Financial Supervision and Supervisory Structure
- Show the weakness both of micro- prudential supervision (soundness or healthy of financial institution) and macro-prudential supervision (results financial instability by macroeconomic shocks)
- Mismatching Problem of Short term debt
- High Leverage Risk of Debt
- High Risk of Hedge Fund and Shadow Banking
- Cross-Border Investment Risk and Spillover Effect of Crisis or Default Risk

Reform of Financial Supervisory Architecture : Arguments

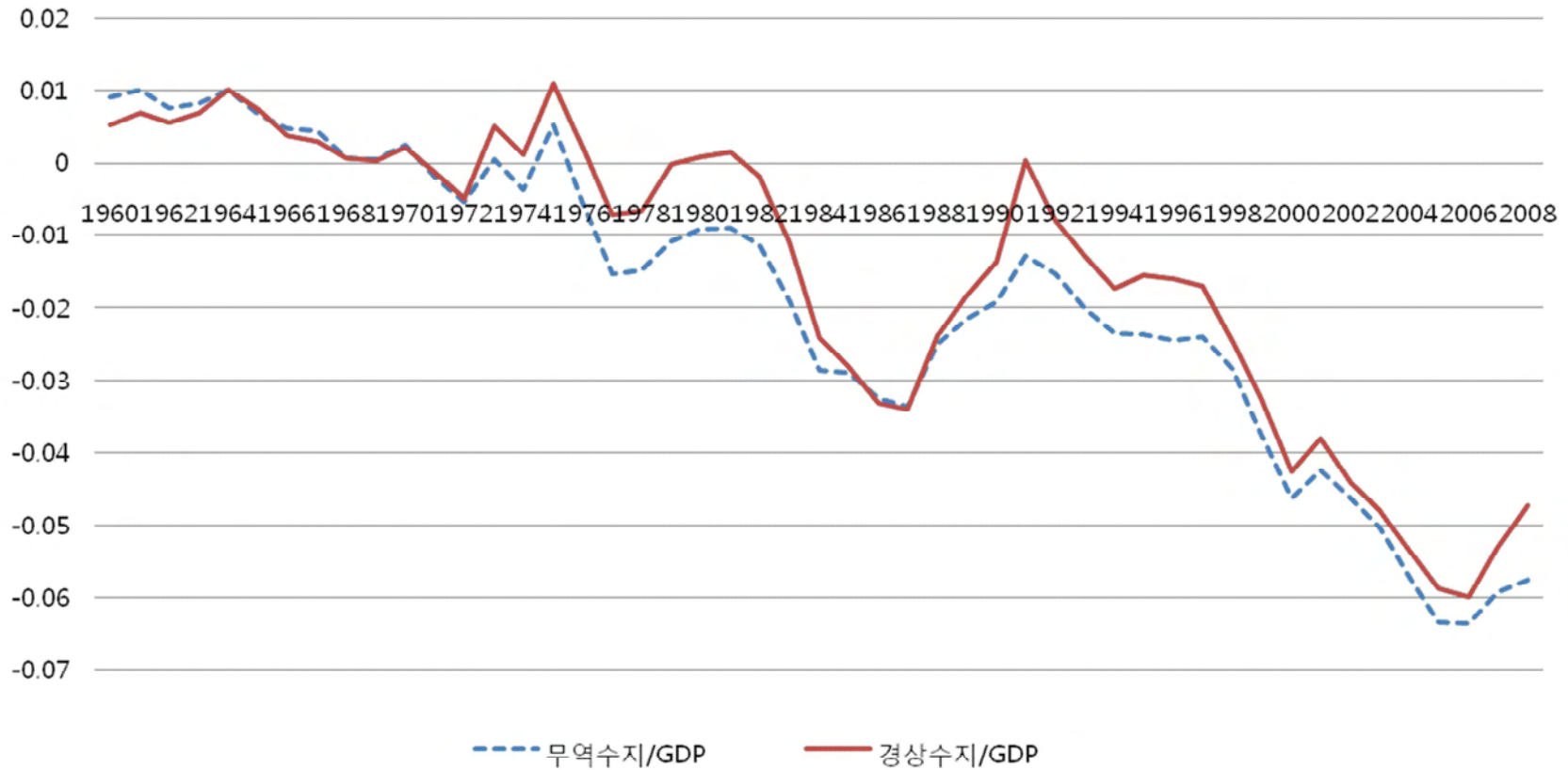
- Unified System or Horizontal System (Twin Peak System)
- Role of Central Bank for Macro-Prudential Supervision
- International or Regional Cooperation of Financial Supervision : Develop Regional Financial Market : Need Cooperation of Financial Supervision
- Financial Regulation of Hedge Fund or Speculative Capital Movement

III. Asian Volatile Financial Environment

- Asymmetric and Vulnerable Real Shocks :
 - Highly Open Economy (Korea : 75%, China : 60%, Japan : 28% : Trade Dependence Ratio)
 - High trade dependency to U.S. and Global Imbalance Problem : Unstable U.S. dollar value

Ratio of (US Trade Deficits/US GDP)

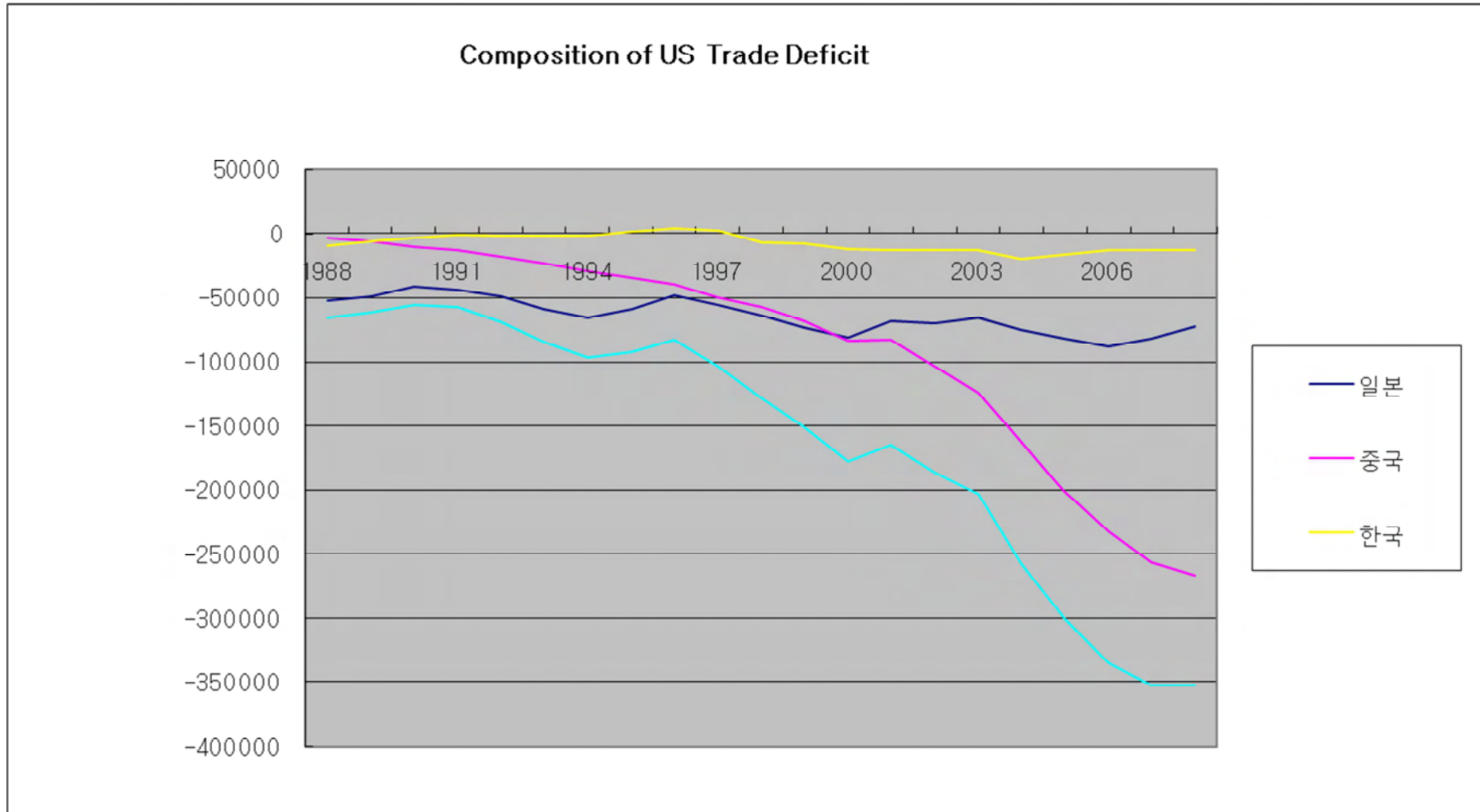
Trend of (US Trade Deficits/US GDP)



Composition of US Trade Deficits

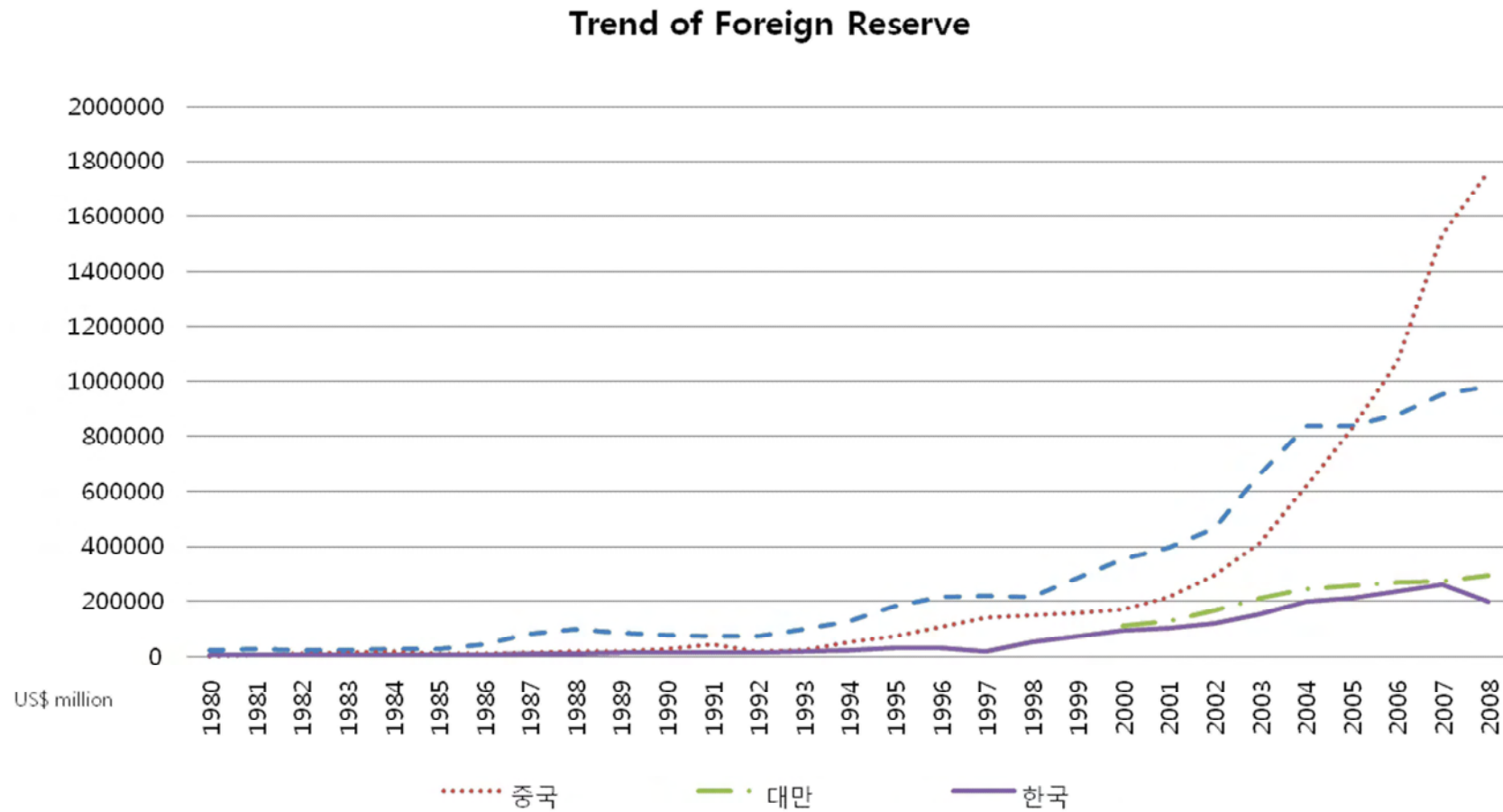
		2008 (US\$ million, %)
Export	Japan	66,579 (5.1%)
	Korea	34,807(2.7%)
	China	71,457(5.5%)
	Total US Export	1,300,135 (100%)
Import	Japan	139,248(6.6%)
	Korea	48,076(2.3%)
	China	377,789(18.0%)
	Total US Import	2,100,141 (100%)
Trade Balance	Japan	-72,669(9.1%)
	Korea	-13,268(1.7%)
	China	-266,332(33.3%)
	Total US Trade Deficit	-800,006(100%)

Composition of US Trade Deficit



- Asymmetric and Volatile Financial Shocks :
 - Korea : Liberalized capital market and non-convertible currency : without adequate foreign reserve, Korea could experiences the recurrent crisis.
 - China : Closed capital market, non-convertible currency and enough foreign reserves(\$2 trillion) : No foreign Exchange Crisis
 - Japan : Liberalized capital market, convertible currency and adequate foreign reserves (\$1 trillion) : No Foreign Exchange Crisis
 - Less Developed Regional Financial Market : Trade surplus in Asia invested to the US and developed countries : Need regional financial cooperation in Asia to develop regional financial market

Trend of International Reserve



Asian Regional Financial Cooperation

- CMI (Chiang Mai Initiatives) in 2000 by (ASEAN+3) : International Reserve Cooperation (Reserve Pooling : Multilateral Swap Agreement) : \$80 billion in 2008
- ABMI (Asian Bond Market Initiatives) in 2003 by (ASEAN+3): Working groups
- ABF(Asia Bond Fund) in 2003 by EMEAP : ABF1 (\$1.025 billion) and ABF2 (\$2 billion)

IV. Restructuring Financial Supervisory System in Korea

- Strengthen Financial Supervision : Macro-Prudential Supervision
 - Stabilize Economy from Frequent Shocks
 - Minimize shocks of the bubble broke-down
 - Establish Financial Stability Committee for Macro-prudential Supervision
 - Develop Early Warning System or Establish Financial Stability Appraisal System

- Strengthen Micro-Prudential Supervision
 - Strengthen Capital and Liquidity Requirement by Basel II
 - More Risk Management
 - Supervise Derivatives Investment
 - Supervise Shadow Banking or Investment banking
 - Leverage Regulation
 - Regulate Pro-cyclical Bank Loan : Buffer Capital Deposit
 - Supervise Moral Hazard of Financial Institution

- Increase Deposit Insurance Limit
- Strengthen Supervisory System of Financial Service Commission(FSC) and Financial Supervisory Service(FSS)
- Strengthen Supervision of International Business : Short Term Debt Management (Supervise Mismatching Problem)
- Need more strong cooperation system among Ministry of Strategy and Finance(MOSF), FSC and Bank of Korea

V. Cooperation of Regional Financial Supervision in Asia

- For Macro Financial Stability : Develop CMI and Activated Bilateral Swap Agreement : To Avoid Foreign Exchange Crisis or Financial Crisis
 - Korea and other Asian countries : Shortage of Foreign Currency
 - Japan and China : Depression of Business Cycle

- To Develop Asian Bond Market :
 - Establish Standard and Global Accounting System
 - Regional Settlement System
 - Credit Guarantee Investment Mechanism(CGIM)
 - Establish Regional Credit Evaluation System
 - Develop Domestic Bond Market

- Cooperation of Regional Financial Supervision
 - Macro Financial Stability Cooperation : Establish Asia Financial Stability Forum : Cross Border Crisis Management
 - Cooperation of Financial Institution's Information
 - Regulation of Short term or Speculative Hedge Fund Capital Movement
 - Cooperation of Supervision for Multi-national Financial Institutions : Establish Regional Supervisory College

Thank you !!