

**Speech by Mr Heng Swee Keat, Managing Director, Monetary
Authority of Singapore,
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Unity And Integration In ASEAN: The Role of The Financial Sector

Mr Wee Ee Cheong, Chairman, ASEAN Bankers Association,

Ambassadors and High Commissioners from ASEAN,

Distinguished guests, ladies and gentlemen,

1. I am delighted to welcome our fellow bankers from ASEAN, and hope that you have a productive and enjoyable stay here. Thank you for inviting me to speak at this ASEAN Banking Conference. The theme of the conference - unity and integration in ASEAN, holds great significance for ASEAN.

A ASEAN ECONOMIES AND BANKING SECTORS HAVE BOUNCED BACK SINCE THE CRISIS

2. Many of you would recall that when the Asian financial crisis struck in 1997/98, critics were asking if our economies and our banking system would crumble, and if the ASEAN grouping would become fragmented. Some mocked that the ASEAN tigers had been reduced to purring cats.

3. Nearly ten years on, ASEAN economies and banking systems have bounced back. This is not by accident but, rather, the result of some painful, hard work. Banks, corporates and governments took tough measures to clean up the balance sheets of ailing corporates, reformed their financial systems, undertook capital market development and strengthened supervision of the financial system. Crucially, ASEAN did not turn inwards. Staying engaged with the global economy has allowed ASEAN to enjoy the recent global economic boom.

4. Bank balance sheets have been restructured and improved over the last few years. Non-performing loans among ASEAN 5 banks have fallen from double-digit highs in 2000 to single-digits in 2005, while net profit margins have improved from a range of 0.4-4.4% to 1.5-6.0% in the same period. These improvements have not gone unnoticed. In 2002, Standard &

Poors gave a negative outlook on half of the banking systems in ASEAN 5 and Vietnam, but in 2006 rated all of these systems as either stable or positive.

5. During this period, ASEAN economies accelerated our regional integration within ASEAN, and pursued integration with our major trading partners. The leaders of both ASEAN and China recently reaffirmed their commitment to complete a full FTA by 2010, while the "early harvest" of this agreement has already been implemented. Today, ASEAN is also negotiating FTAs with other economic centres like Japan, India, South Korea, Australia and New Zealand. ASEAN and the US entered into a Trade and Investment Framework Agreement in August. Individual members of ASEAN continue to pursue trade liberalisation. Vietnam received WTO approval for membership earlier this month. The criss-crossing network of regional and bilateral FTAs is making ASEAN an important "crossroad" between the West, Middle East, East Asia and Oceania.

6. The trade numbers give a glimpse of the degree of integration taking place. Between 2000 and 2005, intra-ASEAN 10 exports grew by 44%. This will grow further as ASEAN brings forward the completion of the ASEAN Economic Community from 2020 to 2015. In the same timeframe, ASEAN's exports to the rest of the world grew by 48%, riding on the growth of China and India. In 2005, ASEAN's trade with China and India amounted to USD 130 billion and USD 22 billion respectively.

7. These numbers reflect important changes in the structural linkages of our economies. A regional production network has developed within ASEAN, and between ASEAN and our regional partners, whereby each economy specialises in one stage of the production chain. This is particularly pronounced in the manufacture of intermediate electronics, downstream oil products and primary commodities.

8. We have become an important manufacturing and commodity hub. For the last three years, ASEAN's GDP grew by a weighted average of 5.8%, exceeding the global growth of 4.8%. In fact, as I noted on a previous occasion, ASEAN's combined GDP of USD 883 billion compares well with India's GDP of USD 772 billion and China's GDP of USD 2.2 trillion, especially when considering that ASEAN's population is less than half of each of these two giants. Based on current growth trends, the combined GDP of ASEAN could reach USD 1 trillion by 2010. So instead of ASEAN economies crumbling, as naysayers predicted, we have bounced back.

B SEIZING OPPORTUNITIES

9. While we have made progress, we must not lose sight of the many problems that remain and the challenges that lie ahead. We need to continue to undertake structural reforms of our economies, strengthen the financial systems and improve the competitiveness of the corporate sectors. We need to improve our laws and policies relating to investment, labour and taxation, and to signal clearly that we welcome foreign investments. Substantial investments are also needed in healthcare, education and infrastructure.

10. I believe there is a great opportunity for ASEAN's bankers to play a key role in all these. As the central intermediaries of credit in the banking system and capital markets, our challenge is to harness the substantial savings within ASEAN and tap into the global capital pool, to finance developments in these areas in a disciplined way. Building on our spirit of co-operation, as bankers and as regulators, we should work more closely together to address current problems, meet coming challenges and seize new opportunities. Allow me to suggest a few ideas.

11. First, how can we be creative yet disciplined in financing SMEs? In ASEAN, SMEs make up more than 90% of all domestic firms and employ 75% to 90% of the non-agricultural domestic workforce. However, their output is only in the range of 20% to 30% of gross sales value or manufacturing value-added, while direct exports make up just 10% to 20% of regional export earnings. Clearly, there is much potential for SMEs to do better. Investments in machinery, in IT, in training of staff, and in developing export markets will be important. The more successful ones will grow, expand and regionalise. For many, the immediate markets of ASEAN will be a logical first-stop, and ASEAN banks can play a helpful bridging role to finance their trade and expansion into new markets.

12. At a macro-level, to sustain growth, all ASEAN economies will need to invest in infrastructure. The demand for infrastructure investment in electricity, water and waste management, roads, ports and telecommunications is particularly large for the economies of Indonesia, Vietnam and the Philippines. Overall, ASEAN's infrastructure needs in the next five years (from 2006 to 2010) are estimated at around USD 50 to 60 billion. As governments cannot finance these alone, private sector participation will be crucial. This provides significant opportunities for regional and global banks to undertake project finance and to facilitate access to the capital markets.

13. With infrastructure finance being treated by global pension funds and asset managers as a separate asset class in its own right, the scope for securitising infrastructure projects has expanded. To encourage greater

diversity of funding options, Singapore recently announced tax incentives to develop the project bond and infrastructure fund markets, as well as incentives to encourage banks to increase their project finance activities. I hope that ASEAN banks, together with global banks operating in ASEAN can work together to consider ways of raising funds for infrastructure finance.

14. More broadly, the development of capital markets, especially the bond market, will enable ASEAN economies to diversify funding options and improve systemic stability. Recently, the Asian Development Bank launched a USD 10 billion multi-currency bond issuance programme. The aim is to help issuers raise local currency funds in multiple markets using a single set of main documents governed under British common law, leaving only the domestic clearing documents under local laws. DBS is the lead manager for the Singapore dollar portion of the issuance and the mandated regional arranger for the programme. ADB has also issued in Thailand - this was arranged by Standard Chartered and Bank of Ayudhya - and I understand that work is underway for similar issuance in other ASEAN economies.

15. It is important to emphasise that the development of capital markets will not be at the expense of banks. Banks already form an indispensable part of the value chain from origination and structuring to pricing, underwriting and placement. By facilitating capital market innovation, banks not only improve access to funding, but also improve the risk profile of their own balance sheets.

16. Moreover, banks also form an important link for investors to access the capital markets. The growth of income and wealth in the region, and the liberalisation of pension savings will create greater demand for financial products. The wide network of branches of ASEAN banks is of strategic value as distribution channels for a range of banking, insurance, mutual funds and capital market products. If ASEAN banks can work together to distribute high quality products suited to their customers' needs, it would help residents in all ASEAN economies to invest their savings appropriately, with proper diversification and returns.

17. A recent trend of significance to ASEAN bankers is the growth of Islamic finance. A recent report by Moody's Investors Service estimates that there are about 300 Islamic financial institutions with over USD 250 billion of assets, growing at 10-15% annually. Another USD 200 billion is estimated to be held in Islamic "windows" of conventional banks. Attracting Shari'ah-compliant deposits is one side of the equation. Being able to invest in a wide-range of Shari'ah-compliant investment vehicles is the other. The number of Shari'ah-compliant financial products is growing - in equities, real estate products, commodities and asset-backed securities.

18. I hope that you will find some time in this conference to explore how ASEAN bankers can work together to further develop Islamic finance. As a regulator, MAS hopes to make a contribution in supporting these developments. We made some recent changes to our regulatory policies, while the Ministry of Finance made changes to the tax policies, to ensure a level playing field and neutrality of rules for both conventional and Islamic financing.

C ASEAN AS AN ASSET CLASS

19. Finally, allow me to touch on the subject of ASEAN as an asset class, a subject much raised by governments and bankers recently. What is an ASEAN asset class? It is about promoting ASEAN as an investment destination. It is about developing a suite of products to help investors understand and include ASEAN assets in their portfolio. It is about drawing up good investment rules and allowing common access to our markets. In short, it is about attracting investors to invest in ASEAN, and to benefit from the ASEAN growth story.

20. Developing an ASEAN asset class is not a one-off government programme. Rather, it is a collective effort, involving banks, corporates, regulators and governments, coming together to design and implement critical initiatives over a sustained period. These initiatives will enable us to collectively build scale and efficiency, in order to be competitive.

21. For example, over the last two years, ASEAN finance ministers have held joint roadshows to promote ASEAN as an investment destination to international investors based in New York, London, Singapore and Hong Kong. As part of this effort, FTSE launched two ASEAN equity indices in September 2005. A year later, CIMB developed one of those indices into an exchange-traded fund (ETF) and listed the fund on the Singapore Exchange. I understand this ETF has done well so far. Under the Asian Bond Fund (ABF) initiative among EMEAP central banks, the ASEAN 5 markets also launched single-market local currency bond funds, which are passively-managed bond funds that provide a low-cost and efficient product for investors to enter individual bond markets. In addition, the ABF helped to accelerate market and regulatory reforms.

22. ASEAN securities regulators recognise the importance of harmonising rules, recognition criteria, standards and practices, as these will help to facilitate investor access across markets and pool the region's opportunities to create a wider range of products for ASEAN savings and a more attractive market for investors. At the same time, ASEAN central bank governors met during the recent IMF/WB meetings in Singapore and reaffirmed their

commitment to support ASEAN's focus on promoting a common market through further liberalisation.

23. The ASEAN working committee on capital market development is now looking at specific ways for the private sector to partner governments to develop an ASEAN asset class. Singapore currently chairs this working committee. I would like to invite all of you to share with us your ideas on developing ASEAN as an asset class. Your ideas will be very valuable in this collective effort.

D CONCLUSION

24. As bankers, I know you have much on your plate - from the implementation of Basel II framework, ensuring good risk management and compliance, to meeting the challenges of banking consolidation and greater competition . Meeting these challenges certainly require first rate leadership and organisational excellence. .

25. Beyond working as individual banks, or as banks in individual countries, we need to work together across ASEAN to achieve scale and depth. The diversity in ASEAN is a strength that can be harnessed. Our track record has shown that while each of our economies and banks may be small by global standards, our collective strength can be substantial whenever we are able to put them together. As in the ten rice stalks that make up the ASEAN logo, unity and integration provides a foundation of strength. May I wish you a most successful conference in deliberating on this theme. Once again, thank you for inviting me for this conference, and may I wish you all a productive stay in Singapore.