

WORKSHOPS



Workshop 3: Development of Domestic and Regional Capital Markets

Workshop Manager: J.H. Park

Topic I: Analysis of Problems and Prospects for Bond Market Development in Asia

It is widely accepted that an important source of the Asian financial crisis that occurred in 1997 was the result of heavy dependence on the banking system for financing domestic investment, and the inefficient functioning of the banking system. Asian countries' financial systems are distinctively bank-dominated. This bank-dominated system had contributed to the fast economic growth prior to the crisis by effectively mobilizing and allocating financial resources to the corporate sector. However, the system caused the corporate sector to over-rely on short-term banking borrowing, which make them very vulnerable to outside shocks. In addition, the massive short-term capital inflows before the crisis aggravated the double mismatch problems, namely a currency mismatch coupled with a maturity mismatch that caused rapid deterioration of balance sheet problems in domestic financial institutions, leading to the crisis. Recognizing the need to develop sound and liquid bond markets in preventing another capital account crisis, countries in the region have exerted increased effort to develop and strengthen bond markets in the aftermath of the Asian financial crisis, drawing on the recent researches undertaken by the ADB Institute.

Session One

Resource Speakers:

Dr. Masaru Yoshitomi, Dean, ADB Institute

*Dr. Sayuri Shirai, Associate Professor, Keio University/
Visiting Scholar, ADB Institute*

*Dr. Charles Adams, Senior Economic Advisor, EDRC,
ADB*

Moderator:

*Dr. Tan Khee Giap, Head, Central Bank Policies
Research Unit, Nanyang Technological University,
Singapore*

This session is designed to first discuss the Nature of the Asian Crisis and the importance of developing sound and viable bond market in preventing another capital account crisis. This will be followed by an analysis of the financial structure in Asian countries and a presentation of an analytical framework for the development of bond market.

Session Two

Resource Speakers:

*Mr. Hidetoshi Mine, Director, Managing Investment
Banking Headquarters, ORIX Corp.*

*Prof. S. Ghon Rhee, Professor, University of Hawaii,
USA*

Moderator:

Dr. Sayuri Shirai, Keio University / ADB Institute

This session will discuss some ways forward to develop international bond markets in the region. The presentations here will concentrate in addressing issues for clarifying the concept of regional bond market, analyzing the benefits of developing regional bond markets, and identifying specific plans for promoting regional financial centers, taking into account the current underdeveloped stage of domestic markets in various countries in the region.

Topic II: Operational and Specific Issues for Developing Bond Market

To develop viable and sound domestic bond markets require continuing and consistent effort to be exerted over a long period of time. And it should cover, among others, formulating policies for broadening the issuer and investor base, and establishing market infrastructure, such as credit rating system, pricing system, benchmark yield curve, regulatory and supervisory framework, and clearing and settlement systems, etc. Sessions Three to Five address these aspects.

Session Three

Resource Speakers:

Ms. Alison Harwood, Principal Securities Market Specialist, IFC

Dr. Sayuri Shirai, Keio University / ADB Institute

Moderator:

Mr. Noritaka Akamatsu, Lead Financial Economist, Financial Sector Development, World Bank

For the bond market development, the role of market participants, such as issuers, investors, and intermediaries should be strengthened, among others. The degrees of market participation will be effected by a range of factors. This session will discuss what those factors are and some of the policies that are needed to influence them. Considering, however, that bank-dominance will continue in the region at least for the short- to medium-term, the role of banks in developing bond market will be analyzed.

Session Four

Resource Speakers:

Ms. Jo Cameron, Manager, Investment Firms Division, Financial Supervisory Agency, UK

Prof. Hideki Kanda, Professor of Economics, Tokyo University

Moderator:

Dr. Charles Adams, ADB

This session will discuss legal and supervisory frameworks for bond market development. Removal of government regulations that discourage bond transactions is indispensable for bond market development. However, more important for bond market development is the establishment of an effective and sound regulatory and supervisory framework. The presentation will emphasize the need to set up a framework to include a set of clearly defined market rules, a high degree of transparency, rigorous prudential standards and governance principles, and internal and external checks and surveillance to monitor compliance with the regulatory framework.

Session Five

Resource Speakers: **Mr. Noritaka Akamatsu**, World Bank
Ms. Cecile Saavedra, Managing Director, Asia-Pacific Ratings, Standard & Poor's
Mr. Prasarn Trairatvorakul, Secretary General, Securities and Exchange Commission, Thailand

Moderator: **Prof. Hideki Kanda**, Tokyo University

This session will discuss important issues on infrastructures for sound development of bond market. Those issues that are discussed in this session include (i) which infrastructures should be established, (ii) how to establish and strengthen the role of credit rating system, (iii) how to improve the clearing and settlement system, and (iv) how to adopt market-based pricing system and create a benchmark yield curve, etc. Establishment of a credit rating system is essential for the development of bond market since it provides investors with objective and independent opinions on the relative risks of bonds, thereby facilitating the transferability of corporate bonds. It also affords bond issuers an incentive for financial improvements, and encourages greater transparency, increase information flows and improve accounting and auditing. Clearing and settlement system is another important infrastructure for bond market development. Settlement system includes institutional arrangements for confirmation, clearance and settlement of securities trades. Considering the diversity of institutional arrangement of each country, presentation will be structured to focus the discussions on the functions to be performed rather than the institutions themselves. Finally, the market-based pricing system and creating the benchmark yield curve will be emphasized as factors for developing sound bond markets.

Topic III: Strategies and Policy Recommendations for the Development of Bond Market

Session Six

Resource Speakers: **Mr. Yun-Hwan Kim**, Senior Economist, EDRC, ADB
Prof. Tan Khee Giap, Nanyang Technological University

Moderator: **Dr. Jae-Ha Park**, Senior Capacity Building Specialist, ADB Institute

Capital markets, including bond markets, in Asia have a high potential for development in the mid- to long-term into effective systems in the sense that the banking sector now accounts for up to 80 per cent of financial assets whereas in the US system, it is 25 percent or less. However, it is expected that it will take time to develop bond markets in the region because of the present poor infrastructures, such as the limited number of qualified bond issuers and also the investor base. In actuality, the supply of quality corporate bonds is very limited in Asia, reflecting the poor credit standing of issuing firms and limited number of large firms with a good reputation. Also the investor base is weak since institutional investors are not well developed and individual investors have strong preferences for liquid bank deposits. Realizing the importance of the need to establish well functioning bond markets in the Asia, the Institute has started research on this issue through the newly established policy forum, the Asian Policy Forum (APF). This session will present strategies and policy recommendations for the development of bond market. In particular, the policy recommendations of APF on how to develop corporate bond markets in the bank-denominated Asian Economies will be presented.