

ASEAN Economic Community (AEC) 2025: Financial Integration in ASEAN

What is AEC 2025?

- Following the establishment of AEC 2015, the AEC Blueprint 2025 has been developed as ASEAN's new master plan for economic integration for the next 10 years. Charting the region's trajectory over the next decade, institutions will be strengthened, commitments followed through with implementation, and monitoring and evaluation enhanced. Unique, dynamic and brimming with potential, ASEAN will assume its aspiring role as a key driver for regional as well as international growth.¹

What is the vision on financial integration under the AEC?

- Under the AEC Blueprint, ASEAN seeks to achieve a well-integrated and smoothly functioning regional financial system, characterized by more liberalized capital account regimes and inter-linked capital markets.

How will the three strategic objectives of the 2025 Financial Integration Vision be implemented?

- Under the AEC Blueprint 2025, the financial sector integration vision for 2025 encompasses three strategic objectives, namely financial integration, financial inclusion, and financial stability, and three cross-cutting areas (Capital Account Liberalization, Payment and Settlement Systems, and Capacity Building).
- Strengthening of financial integration aimed at facilitating intra-ASEAN trade and investment will be implemented through increasing the role of ASEAN indigenous banks, and having more integrated insurance and capital markets. These will be supported by a robust financial market infrastructure that is safe, cost-efficient and more connected.²
- Promoting financial inclusion will be done through the delivery of financial products and services to a wider community that remain underserved, including micro, small and medium enterprises (MSMEs). This would also include initiatives to address the uneven digital gap in the region and reflect changes in the demographic structure as some countries become aging societies.³
- Financial stability will be ensured through the continuous strengthening of regional infrastructure, particularly in times of regional stress.⁴

What are the specific areas of financial integration? How will these be achieved under the AEC? What are the accomplishments so far?

- Financial integration in ASEAN will be accomplished in the following specific areas:
 - a. *Financial Services Liberalization (FSL), including Banking Integration.* The gradual removal of restrictions on ASEAN banks, insurance companies and investment companies in providing financial services in other ASEAN Member States (AMS) will be implemented. AMS meet and negotiate on what financial services each country is willing to liberalize during the specified period. The process of liberalization takes into consideration the readiness of the member

¹ ASEAN Economic Community 2015: Progress and Key Achievements (2015)

² ASEAN Economic Blueprint 2025

³ Ibid

⁴ Ibid

economies, with an aim to have freer flow of financial services (subject to pre-identified flexibilities). In banking, AMS target the operation of Qualified ASEAN Banks (QABs), which shall be accorded equal treatment as the domestic banks in the host jurisdiction, in each of the ASEAN member economies.

To date, seven (7) rounds of negotiations of FSL have been completed. The ASEAN Banking Integration Framework, which states that AMS will work towards allowing entry of QABs in the region, has been approved (details on page 5).

- b. *Capital Account Liberalization*. ASEAN aims to achieve freer flow of capital by gradually removing restrictions on foreign exchange transactions such as those in the current account (CA), foreign direct investments (FDIs), portfolio investments (PIs) and other flows (OFs), while imposing adequate safeguards.

To date, assessment and identification of rules of AMS on foreign exchange transactions have been completed. Individual roadmaps, which show member countries' plans to progressively liberalize their capital account regimes, have been drafted. Policy dialogue mechanisms were also established to keep track of the current trends in capital flows and exchange information on capital flow management measures, if any, among the ASEAN economies.

- c. *Capital Market Development (CMD)*. ASEAN also focuses on developing, interlinking and deepening the region's capital markets by building capacity and laying the long-term infrastructure to achieve integration of capital markets in ASEAN. This will be implemented through harmonization of domestic laws and regulations and linkage of market infrastructure.
- d. *Harmonized Payments and Settlement Systems (PSS)*. ASEAN aims to establish an ASEAN payment system that is safe, innovative, efficient and more interconnected. It will be achieved through the adoption of international standards in domestic payment systems, development of domestic retail payment system and more efficient remittance mechanism, sound consumer protection and adequate risk management, among others.

Accomplishments include the development of Basic Principles on the Pre-Departure Orientation Program for migrant workers and adoption of ISO 20022⁵ messaging format for credit transfer scheme, among others.

- e. *Financial Inclusion (FINC)*. ASEAN deliberates policy options, engage stakeholders and coordinate collective actions by member countries to enhance financial inclusion in ASEAN in the areas of financial intermediaries and distribution channels, financial education, and consumer protection.

Milestones to date include, among others, completion of frameworks for FINC, financial education, and consumer protection, as well as capacity-building programs in various areas of financial inclusion including FinTech, data and strategy, impact assessment and credit guarantee.

- f. *Capacity Building*. ASEAN recognizes the need to provide necessary capacity building and other initiatives to narrow the development gaps among ASEAN economies and bring all AMS to fully participate in the ongoing integration efforts. ASEAN coordinates the matching of capacity-

⁵ ISO 20022, also called Universal financial industry message scheme (UNIFI), is the international standard developed for financial messages. Its business modelling approach allows users and developers to represent financial business processes and underlying transactions in a formal but syntax-independent notation. It is used by financial institutions that want to streamline their communication infrastructure and limit associated costs (Source: ISO 20022 webpage).

building needs and possible suppliers; development of learning programs; and identification of funding requirements.

Learning programs have been conducted for Brunei Darussalam, Cambodia, Lao PDR, Myanmar and Vietnam (BCLMV). ASEAN continues the development/coordination of learning roadmaps for specific financial integration areas (CMD, CAL and PSS). ASEAN has also engaged partner institutions on funding arrangements to support the implementation of capacity-building programs.

Is there a work plan/program to achieve the goal in 2025?

- Each sector involved in the ASEAN integration efforts has prepared its work plan in the form of a Strategic Action Plan (SAP) to guide its efforts towards 2025. The comprehensive SAP of the financial sector, which has been categorized according to three pillars: Financial Integration, Financial Inclusion, and Financial Stability, has been approved by the ASEAN Finance Ministers' and Central Bank Governors' Joint Meeting (AFMGM) in April 2016 and posted in the ASEAN website.⁶
- To keep track of the initiatives under the SAP, the AMS also developed Key Performance Indicators (KPIs) which aim to measure whether regional economic integration objectives and outcomes are achieved by a sector. During its meeting on 7 April 2017, the AFMGM endorsed the adoption of KPIs by the Working Committees.
- The overall monitoring of the implementation of strategic measures, impacts and outcomes of the AEC Blueprint 2025 shall be conducted by the ASEAN Integration Monitoring Directorate of the ASEAN Secretariat (ASEC).

What are the roles of the ASEAN Finance Ministers and Central Bank Governors, and their Deputies, in the implementation of initiatives on financial integration?

- The ASEAN Finance Ministers and Central Bank Governors provide guidance and direction in the implementation of the work programs of the different working committees/task forces on financial integration.
- The *Senior Level Committee (SLC) on ASEAN Financial Integration*, composed of Central Bank Deputies/Senior Central Bank Officials and Chairs/Co-Chairs of the different working committees, plays a critical role in ensuring the implementation of key milestones and timelines of financial integration in the region since 2011. The SLC identifies and monitors macroeconomic and financial stability risks and its impact on the ASEAN financial integration agenda. The SLC also engages international financial institutions to enhance discussions on recent economic and financial market developments and risks to the outlook.
- While the SLC and the Central Bank Governors/Deputies focus on issues concerning central bank functions (banking integration, capital flow liberalization, payments and settlement systems), the Finance Ministers/Deputies provide guidance on the sectors under their jurisdiction such as insurance services, securities markets, taxation, and customs, among others.

⁶ <http://asean.org/storage/2012/05/SAP-for-Financial-Integration-2025-For-publication.pdf>.

What other initiatives are available to support the financial integration agenda in the region?

- ASEAN and ASEAN+3 countries (China, Japan and Korea) also pursued several initiatives to support the financial integration agenda in the region such as the following:
 - a. *Financing arrangements.* To assist countries with short-term liquidity difficulties, AMS established the US\$1 billion ASEAN Swap Arrangements (ASA) in August 1977. The ASA was later increased to US\$2 billion in 2005, to enhance its credibility and usefulness, upon the signing of a Memorandum of Understanding (MOU) among AMS. The MOU has been renewed five times, the latest of which was signed in October 2015 renewing the ASA for two more years. The Chiang Mai Initiative Multilateralization (CMIM), a US\$120 billion multilateral currency swap facility was launched in March 2010 and designed to assist countries with short-term liquidity difficulties. The amount of the CMIM facility was doubled to US\$240 billion in May 2012.
 - b. *Surveillance and policy dialogue.* The ASEAN Integration Monitoring Directorate of the ASEC is responsible for the overall monitoring of the implementation of strategic measures, impacts and outcomes of the AEC Blueprint 2025. The ASEAN+3 Macroeconomic and Research Office (AMRO) was incorporated in April 2011 and started operations in May 2011 to serve as the independent regional surveillance unit of the CMIM. The AMRO was converted into an international organization in February 2016.

What are the benefits for and risks to the Philippines in engaging in financial integration in ASEAN?

- The ASEAN financial integration will generally enhance the overall health of the Philippine financial sector, and contribute to further growth and resiliency of the economy. The following are the major benefits of financial integration:
 - Freer flow of trade in services allows ASEAN services suppliers to provide services, including financial services (e.g., banking services, insurance services, investment facilitation) and establish companies across national borders within the region, subject to domestic regulations. This will result in the offering of a broader range of financial services, including micro-financing and insurance, available to a larger consumer base.
 - With freer flow of capital, economic agents in any member state will be able to invest in or borrow funds more freely (or subject only to prudential regulations) from any other member state.
 - With integrated capital markets in ASEAN, AMS can expect improved access to capital markets, establishment of necessary market infrastructure, lower transaction costs, and more efficient business processes.
 - Under a vision of having a harmonized ASEAN payments and settlement systems, businesses and individuals will be able to make or receive electronic payments with greater convenience and security.
- It is recognized that despite the benefits of financial integration, the interdependence of financial markets increases the risks of contagion. For instance, if one financial institution or a particular AMS in the region is initially affected by a problem or a crisis, under an integrated financial market, this may spread to the rest of the financial sectors of other countries. Hence, as countries in the region open and integrate their financial markets, it is important to establish the necessary capacities; pursue sound and consistent macroeconomic policies characterized by price stability and fiscal

discipline, in order for AMS to fully maximize the benefits and outweigh the risks of an ASEAN integrated financial markets.

ASEAN Banking Integration

Can foreign banks operate in the Philippines?

- Yes, Republic Act (R.A.) No. 7721 as amended by R.A. No. 10641, enacted on 15 July 2014, allows foreign banks to operate in the Philippines through any one of the following modes of entry, subject to relevant licensing and other requirements prior to actual entry:
 - a. Establishment of foreign bank branches with full banking authority;
 - b. Acquisition of up to 100 percent of the voting stock of an existing domestic bank; or
 - c. Investing in up to 100 percent of the voting stock of a new locally incorporated banking subsidiary.

What is the ASEAN Banking Integration Framework (ABIF)?

- ABIF is a framework agreed upon among the AMS to facilitate the entry and operation of Qualified ASEAN Banks (QABs) in other ASEAN countries to promote equal access and treatment among ASEAN banks and facilitate the expansion of intra-regional trade. QABs are high quality banks that meet specific qualifications including the prudential requirements of host countries.

How can ABIF facilitate regional banking integration and market access in each AMS?

- Based on the stage of development and readiness, two or more AMS may negotiate and agree on reciprocal arrangements for the admission of and grant of flexibilities to QABs in their respective jurisdictions. The guidelines/arrangements for the entry of QABs will respect domestic laws and licensing requirements of the host countries.

How does R.A. No. 10641 relate to ABIF? What is the difference between R.A. No. 10641 and ABIF?

- R. A. No. 7721 as amended by R.A. No. 10641 are the governing laws for the entry of all foreign banks whether ASEAN or non-ASEAN banks. Together, these laws provide the legal framework to enable the Philippines to participate and implement the ABIF. With these laws as guide, the BSP may engage in bilateral ABIF negotiations with other AMS to agree on reciprocal arrangements that will facilitate the entry of Philippine banks in the other AMS, and entry of banks from one AMS into the Philippines.
- ABIF focuses on the entry and operation of QABs and promotes cooperation and mutual support. The ABIF provides the framework to facilitate banking integration and support the growth of ASEAN banks particularly those from Brunei Darussalam, Cambodia, Lao PDR, Myanmar and Vietnam. ABIF encourages more meaningful concessions through bilateral arrangements that are mutually beneficial to parties with the view of enhancing opportunities for banks and reducing market access gaps. To achieve these goals, ABIF also provides for the development for capacity building-programs and home-host financial stability arrangements.