

Promoting the Use of Local Currencies

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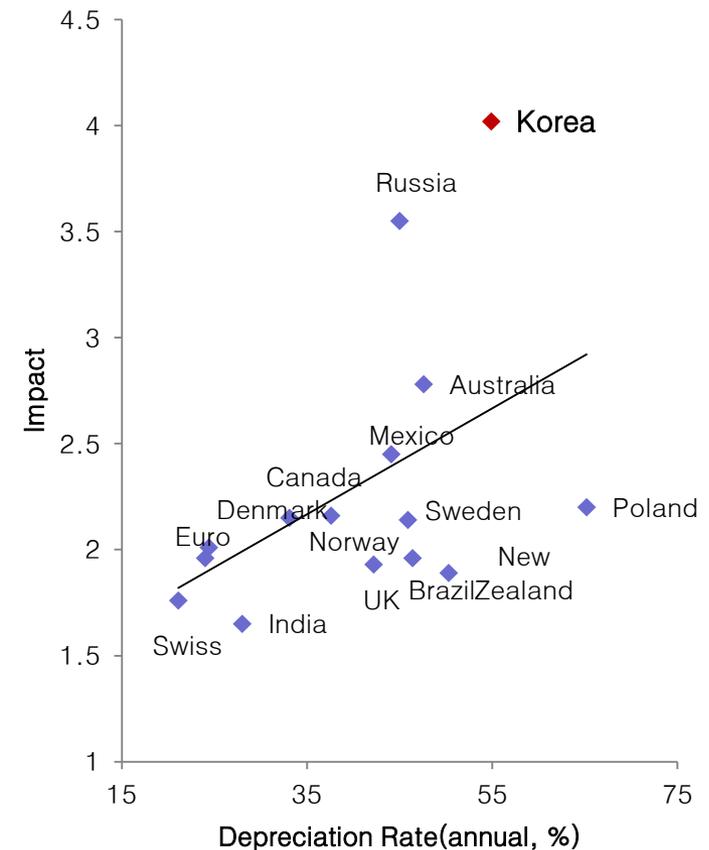
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Common Theme: Need for financial cooperation among Asian countries

❖ As we experienced, global liquidity risk spread to EM thru FX market

Area	Economy	Jul07-Jun09 % change vis-a-vis USD	JP Morgan REER Jul07-Jun09 % change	Jun97-Jul98 % change vis-a-vis USD	JP Morgan REER Jun97-Jul98 % change
asia	Korea	-28.6	-25.7	-27.8	-13.2
latam	Mexico	-16.7	-14.3		
cee	Turkey	-16.3	-11.7		
asia	India	-15.6	-11.1		
cee	Poland	-12.6	-10.9		
asia	Philippines	-5.6	-8.0	-37.2	-25.2
latam	Argentina	-18.0	-5.2		
asia	Singapore	4.1	-3.0		
cee	Hungary	-6.0	-1.6		
asia	Thailand	-0.6	-1.4	-36.8	-15.7
asia	Hong Kong	0.9	-1.0		
latam	Colombia	-9.9	-1.0		
cee	Russia	-18.2	3.2		
latam	Chile	-1.1	4.1		
latam	Peru	5.0	5.1		
africa	South Africa	-7.8	5.6		
asia	China	10.8	6.5		
latam	Brazil	-3.6	7.0		
asia	Malaysia	-2.0	10.6	-39.1	-24.5
asia	Indonesia	-9.9	18.7	-81.2	-64.4
latam	Venezuela	0.0	54.5		
	<i>Emerging Asia, average</i>	-5.2	-1.6		
	<i>Non-Asian OEMs, average</i>	-8.8	2.9		



Low degree of intra-regional financial transaction



- ❖ The region's abundant savings are used mainly to hold US treasuries or other safe assets; intra financial trading is very low

<Risk-sharing in the region (1998-2005)>

Post-Crisis Period (1998-2005)

	JP	ROK	CH	HK	TW	ID	MY	PH	SG	TH	US	UK	EU
JP	1												
ROK	0.724	1.000											
CH	-0.453	0.212	1.000										
HK	0.854	0.639	-0.240	1.000									
TW	0.748	0.592	-0.372	0.528	1.000								
ID	0.547	0.886	0.264	0.635	0.405	1.000							
MY	0.557	0.835	0.314	0.761	0.445	0.931	1.000						
PH	0.801	0.601	-0.543	0.595	0.820	0.580	0.469	1.000					
SG	0.925	0.742	-0.269	0.956	0.737	0.657	0.765	0.714	1.000				
TH	0.274	0.713	0.409	0.398	0.352	0.842	0.811	0.391	0.457	1.000			
US	0.755	0.647	-0.201	0.840	0.490	0.737	0.724	0.745	0.788	0.495	1.000		
UK	0.856	0.304	-0.724	0.711	0.639	0.145	0.189	0.712	0.731	-0.132	0.666	1.000	
EU	0.713	0.563	-0.408	0.499	0.546	0.539	0.364	0.855	0.538	0.196	0.793	0.693	1.000

Source: World Federation of Exchanges

Asian Financial Cooperation Status: at the government & central bank level

❖ ASEAN (1967-)

- Indonesia, Malaysia, Philippines, Singapore, Thailand, Brunei, Myanmar, Cambodia, Laos, Vietnam

❖ ASEAN+3 (1999-)

- ASEAN + Korea, Japan, China

❖ SEANZA (1956-)

- South East Asia(17) + New Zealand and Australia

❖ SEACEN (1982-)

- South East Asian Central Banks(17)

❖ EMEAP Governors and Deputies Meeting (1991-)

- Central banks and monetary authorities in East Asian and Pacific region(11)
- Indonesia, Korea, Malaysia, Philippines, Singapore, Thailand, China, Australia, Hong Kong, Japan, New Zealand

❖ **Chiang Mai Initiative (CMI)**

- Network of currency swap arrangement among ASEAN+3 member countries (2001)
- The initial bilateral arrangement were transformed into multilateral form in May 2009 (effective since March 24, 2010)

❖ **Economic Review and Policy Dialog (ERPD)**

- Aim to detect irregularities and vulnerabilities early
- Annual ministerial meeting & biannual deputies meeting

❖ **Asia Bond Market Initiative (ABMI)**

- Aim to develop local currency-denominated bond market
- 4 working groups launched
 - Developing new securitized instrument; Establishment of regional credit guarantee mechanism; Developing Asian settlement system; Strengthening Asian credit rating agencies

Key initiatives under EMEAP – ABF

❖ Asia Bond Fund (ABF)

- Demand side stimulus from purchases by central banks of sovereign bonds using foreign exchange reserves

	ABF 1	ABF 2
Start of Investment	July 2003	March 2005
Investment Style	Passively managed against designated benchmark indices	
Total Amount	USD 1 billion	USD 2 billion
Qualifying Assets	<ul style="list-style-type: none">• Sovereign and quasi-sovereign bonds issued in 8 EMEAP economies• Denominated in USD	<ul style="list-style-type: none">• Sovereign and quasi-sovereign bonds issued in 8 EMEAP economies• Denominated in domestic currencies
Fund Manager	BIS	Private
Investors	EMAP central banks	Phase 1: EMEAP central banks Phase 2: other public and private sector investors

Many progresses have been achieved

❖ Major Achievements:

- Emergency Liquidity Provision
 - CMI → CMIM: promptly activated through collective decision making process
 - Recently, ASEAN+3 finance ministers endorsed the proposed doubling in size of CMIM programme to \$240 billion
 - Compulsory link to IMF bailout condition also reduced
- Regional Bond Market Development
 - ABMI : Discussion of CGIF
 - ABF1→ABF2: increased momentum in cooperation

❖ Major achievements(CMI/CMIM, ABMI, ABF) are good starting point of for further deepening of regional financial cooperation

Still, most of international transactions in the region uses *foreign* currency...

❖ USD is the dominant currency in the international transaction while intraregional trade has been dominating.

- (Store of value) 61.8% of foreign reserves
- (denominated currency in the international bond market) 39% of international bonds issued in 2010
- (FX transaction) 42.4% (2010, BIS Survey)

Korea's Export by region (%)

	2002	2004	2006	2007	2008	2009	2010
US	20.2	16.9	13.3	12.3	11.0	10.4	10.7
Europe	16.6	17.6	18.5	19.2	18.2	15.4	14.9
Asia	47.6	51.0	51.8	50.8	50.7	52.5	54.7
(Japan)	9.3	8.5	8.2	7.1	6.7	6.0	6.0
(China)	14.6	19.6	21.3	22.1	21.7	23.9	25.1
Others	15.6	14.5	16.5	17.7	20.1	21.8	19.7
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0

KRW in International trade settlement

Invoicing currencies of Korea's Export (%)

	USD	Euro	Yen	Won	Yuan	Others
2006	79.6	8.8	4.8	0.6	0.002	6.2
2007	77.2	9.6	4.6	0.7	0.003	8.0
2008	81.6	7.6	4.6	0.8	0.005	5.3
2009	85.4	6.7	4.3	0.8	0.009	2.7
2010	85.9	6.0	4.4	1.1	0.053	2.6
2011	86.2	5.6	4.1	1.5	0.194	2.4

Invoicing currencies of Korea's Import (%)

	USD	Euro	Yen	Won	Yuan	Others
2006	80.9	5.2	11.2	1.7	0.004	1.0
2007	80.7	5.6	10.8	1.8	0.008	1.0
2008	82.0	5.8	9.7	1.6	0.011	0.8
2009	80.1	6.3	10.1	2.3	0.015	1.1
2010	81.3	5.4	9.9	2.4	0.023	1.0
2011	82.9	5.1	8.0	3.2	0.022	0.8

Promoting foreign trade settlements in local currency

❖ **Benefits of using a local currency in trade settlement**

- Trade competitiveness of the region will be less impacted by fluctuations of non-regional currencies
- Trade finance become easier, as the impacts from the liquidity conditions of non-regional currencies would become less
- Settlement risk would be reduced

❖ **Stylized facts on invoicing currency for trade**

- Trades between developed countries tend to be invoiced in exporter's currency
- Trades between a developed country and a developing country tend to be invoiced in the developed country's currency
- Differentiated products tend to be invoiced in the exporters currency
- Commodities, such as crude oil, are invoiced in an international currency

Pre-conditions to become an invoicing currency



❖ Theories show many factors affect the choice of an invoicing currency

	US	JPN	EU	UK	AUS	SW	KOR	CHN
Trade (% of world total)	10.7	4.8	12.7	3.2	1.4	1.2	2.9	9.8
GDP (% of world total)	23.1	8.7	19.3	3.6	2.0	0.8	1.6	9.3
National Deb to GDP (%)	94.4	220.0	85.8	75.5	20.5	54.5	33.4	33.8

% changes of selected currencies (year-to-year, against USD)

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
JPN	-11.3	-3.1	8.2	7.2	-1.8	-5.2	-1.2	13.9	10.5	6.6
EU	-2.9	5.2	19.9	10.0	0.2	0.9	9.1	7.0	-5.2	-4.7
UK	-4.9	4.1	8.9	12.1	-0.7	1.2	8.7	-8.1	-15.3	-0.8
AUS	-10.8	5.0	19.4	13.4	3.8	-1.4	11.1	0.2	-7.0	17.6
SW	0.1	8.3	15.7	8.3	-0.1	-0.7	4.4	10.8	-0.5	4.3
KOR	-12.4	3.2	4.9	4.2	11.7	7.2	2.8	-15.8	-13.6	10.4
CHN	0.0	0.0	0.0	0.0	1.0	2.8	4.8	9.5	1.7	0.9

Growing role of Asian & EM currencies

❖ Strong Fundamentals are needed

- Empirically, economic weight, trade centrality, macroeconomic stability and financial depth are contributing factors to wider international use of a currency
- Relative importance vary across currencies

	Brazil	China	Hong Kong SAR	India	Indonesia	Korea	Mexico	Russia	Singapore	South Africa	Turkey
Macro indicators											
GDP size ²⁾	3.6	10.9	0.4	2.8	1.3	3.2	1.7	1.7	0.4	0.6	1.2
Economic growth ³⁾	4.2	9.5	4.4	8.1	6.7	4.2	3.6	4.3	4.4	4.2	4.2
Inflation ⁴⁾	4.9	2.6	3.4	5.2	4.9	3.3	3.1	7.2	2.5	5.0	5.2
Sovereign ratings ⁵⁾	BBB-	AA-	AAA	BBB-	BB+	A	BBB	BBB	AAA	BBB+	BBB-
Capital account openness ⁶⁾	0.4	-1.1	2.5	-1.1	1.1	0.4	1.1	0.2	2.5	-1.1	0.1
Total trade ⁷⁾	1.3	11.0	2.7	2.3	0.9	3.1	1.8	2.3	2.6	0.5	1.0
Exchange rate flexibility ⁸⁾	Floating	Crawl-like arrangement	Currency board	Floating	Floating	Floating	Floating	Other managed	Other managed	Floating	Floating
financial indicators											
Financial depth ⁹⁾	1.6	7.2	1.6	1.1	0.3	1.2	0.5	0.8	0.5	0.5	0.4
Intl. debt securities ¹⁰⁾	0.1	0.1	0.2	0.0	0.0		0.1	0.1	0.1	0.1	0.1
FX market turnover ¹¹⁾	0.3	0.4	1.2	0.5		0.8	0.6	0.5	0.7	0.4	0.4
FX bid-ask spreads ¹²⁾	8.6	1.7	1.2	6.7		11.6	7.2	7.9	6.7	31.2	23.6

Promoting the use of KRW/RMB in international trade

❖ KOR-CHN economic relationship

- China is the biggest trade partner of Korea / Korea is the 3rd largest of trade partner of China
- Bilateral trade USD \$245.6 billion (2011) / expect to reach USD \$300 billion by 2015
- KOR-CHN FTA negotiation has been launched

❖ Use of KOR-CHN currency swap to promote the use of KRW/RMB

- 64 trillion won / 360 billion RMB in size (2011.10)
- Aims to provide emergency liquidity provision, also aim to **boost bilateral trade**
- Device needed to provide hedging and settlement facility for exporters/importers