Competition and change in **Asian infrastructure**

Advancing critical dialogue

Can the commercial sector lead the way in market infrastructure reform?

Does the absence of a single Asian currency matter?

What is driving individual reform initiatives?

Despite the absence of a common currency, common standards and regulatory pressure towards cooperation across borders, Asia feels much like Europe did in the run-up to the 2002 publication of the original SEPA Roadmap. There may be a history of fierce competition between Asian markets that can hinder effective cross-border dialogue, but there is also high-level enthusiasm for market harmonisation and the removal of cross-border barriers as well as a widespread belief that there will be significant change over the next few years. "These are issues that warrant a high priority," says Esmond Lee, head of the market systems development division at the Hong Kong Monetary Authority, in a discussion of current planning at the HKMA. "In 2009, when Sibos is in Hong Kong, we will have something much more concrete to discuss," Lee adds.

There are two principal drivers for such harmonisation. While competing among themselves, each market is keenly aware of the need to remain relevant in a global sense. Tokyo, Hong Kong and Singapore not only have one eye on each other; they also have an eye on the EU and US. At the same time, many Asian financial institutions have operations in a number of countries in the region and are faced with the challenge of streamlining diverse processes, systems and compliance requirements.

There is even talk in some circles of an Asian Currency Unit. While it is conceded that this is a long way off, the point is also made that Asia already has an effective proxy for a single currency in the US dollar. And in many sectors, there is a business case for change. Speaking at Sibos in Boston on Asian capital-market reform, Shigehito Inukai, director of policy studies and senior fellow, National Institute for Research Advancement, Japan, asked, "Why is it that Asian issuers need to raise capital in London or

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New York whilst there are huge Asian capital reserves?" Inukai proposed the integration of Asian capital markets as an alternative to London and New York.

But for many, Europe remains the compelling precedent. Discussions of Asian infrastructure reform typically include reference to the Single Euro Payments Area (SEPA), in much the same way that discussions of SEPA have always tended to bring in Check 21 and other US precedents. It is as if a wave of harmonisation is widely expected to spread from west to east across the globe.

If it does, it will be an impact of globalisation. "Markets in the region are realising more and more that to be competitive in the global market, they need to provide a safe and efficient environment in which to do business," says Patrick de Courcy, head of markets and solutions, Asia Pacific, SWIFT.

"That translates directly into the very practical steps that many of them are taking now to make their infrastructures as open as possible to the outside world." Examples from the securities arena include SWIFT's recent signing of a memorandum of understanding (MoU) with JASDEC to work with the Japanese depository towards adopting ISO 20022 standards; an MoU with the Shanghai stock exchange on adopting ISO standards for corporate actions; and an MoU with the Singapore stock exchange on implementing an ISO-based pre-settlement matching system. Euroclear has also recently signed MoUs with one CSD in India and two in China.

National focus

While these are responses to external pressure, they are still national rather than regional initiatives. "You have to be very careful about trying to characterise Asia as being homogeneous in any way," notes Philip Reichardt, director and head of international cooperation at Euroclear. "There are tremendous rivalries and lots of competition." Markets may be advancing, but they are advancing in competition with each other, rather than in cooperation. This is not necessarily bad news, however. "As a result, you find that the infrastructure in many countries is actually quite advanced," says Reichardt. "Competitive pressure has meant that they have taken full advantage of technology." Advances are particularly marked in trading, risk management and settlement, Reichardt adds, though stressing the significant differences between markets.

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Professor Masashi Nakajima, International School of Economics and Business Administration, Reitaku University

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Matthew Marks, Financial Services Industry marketing manager, Asia-Pacific, Sterling Commerce

The significance of this technological advancement in not-yet-open markets is that it enables leapfrogging. Describing meetings in Asia spent answering questions about Europe, Reichardt says, "If a market can adopt the standards that have evolved in European markets, it can leapfrog the very, very long time that it took the Europeans to get to where they are today." While it is true that easing currency controls and opening up a market to international investment and competition are not simple steps for a government to take – raising political and cultural as well as economic issues – it is also true that if a market is already capable of meeting international standards, that step will be at least a degree easier. "It is pull and push," comments Reichardt. "If the infrastructure already accommodates international standards, the policymakers can see that their job won't be so difficult."

The Korean example

If a market's infrastructure has already learned the lessons of the Europe experience, there is every likelihood that the 'new' international market will hit the ground running. Asia's leading markets are already high up the learning curve that opening borders, breaking down barriers, removing currency controls will entail. There is pressure for harmonisation, and grounds for believing that when it does come, the transition period will be short.

This is an across-the-board evolution. In Korea, for example, SWIFT has signed an MoU with the Korea International Trade Association (KITA) and Korea Exchange Bank (KEB) to "develop integrated services that will facilitate Korea's international trade". Korea's uTradeHub paperless system already links 80,000 member companies of KITA with their banks for document exchange, but although it has dematerialised, uTradeHub is still built around the letter-of-credit process. It is also domestic.

The aim here is to explore synergies between KITA's uTradeHub and SWIFT's Trade Services Utility (TSU) to leverage what Korea already has on an international scale. "We aim to bring together SWIFT's global coverage and the TSU and KITA," says De Courcy. "It will be a match made in heaven for banks and exporters in

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Korea and it is a model that could be adopted in other countries." Similarly, Michael Kang, senior manager of trade and services at KEB, says, "This is a win-win strategy and it will enable the national platform to develop new customers."

As this initiative suggests, in trade as in other sectors, the drive to upgrade national infrastructures is beginning to develop an international dimension. But the SWIFT/KITA/KEB initiative also supports another contention: that the absence of any centralised driving body equivalent to the European Commission or other central regional authority is not a barrier to harmonisation. If there is a central space in Asia that needs to be filled, the contention is that it has already been filled. Europe's single currency, single market and single payments area may have been driven from the centre by regulatory pressure, and Asia may lack that driver, but there is an equivalent pressure in the form of the "pull and push" between the region's keen students of the European example and such bodies as SWIFT and Euroclear bringing their euro-experience to bear on the region. There are enough MoUs being signed in Asia now to make up for the lack of any directives from the centre.

The question is not whether Asia can harmonise without a central regulatory driver. If Asia can learn from observing the European experience, and if the private sector can import the practical know-how and technical expertise represented by the centre (albeit without the regulatory/legislative component), the issue surely is: will Asia's private-sector harmonisation take as long as the equivalent centrally-driven process took in Europe?

The role of the regulators

There may be no precedent for a private-sector-led regional market harmonisation, but perhaps there is about to be one. The case against rests on two points. First, there is not a critical mass of intra-regional activity nor compliance with international standards to drive change (44% of all MT700s – issues of a documentary credit – transported over SWIFT are intra-Asia-Pacific), and secondly, the region's non-homogeneity and competition between markets prohibit cooperation. But for Professor Masashi Nakajima of the International School of Economics and Business Administration at Reitaku University, these are not insurmountable obstacles. "There is a belief that there should be a unifying regulatory driver towards reform," he says, "but the EU was a special case in that the single currency made SEPA necessary and inevitable. Asia is very different. In Asia, competition between markets will play a big role in driving reform."

For Nakajima, the key point is that Asian markets are externally oriented, beyond Asia. Effective competition thus means complying with global standards. Those standards are, therefore, fed back into the region. Asian market infrastructures will be harmonised by their counterparties. And as Matthew Marks, Financial Services Industry marketing manager, Asia-Pacific, Sterling Commerce, points out, Asia's markets are beginning to develop distinct and separate areas of expertise; this may take them beyond competition and into cooperation. "Hong Kong has positioned itself to do US dollar and Euro settlements in the Asian time zone, connecting to RTGS systems across the region. Singapore is trying to establish itself as a wealth-management and funds centre, while Kuala Lumpur has positioned itself as the Islamic banking centre for the region," Marks says. Asia is becoming a multiple-stop shop.

Roughly half a decade has passed since the SEPA Roadmap was published. Sibos opens in Hong Kong in a little less than two years. How far Asian market infrastructures will come to res emble each other in adopting global templates without a regulatory driver is a matter of keen interest for sceptics and optimists alike.