

THE AUSTRALIAN
APEC STUDY CENTRE



Asia-Pacific
Economic Cooperation



Submission to Australia's Financial System Inquiry

The Australian APEC Study Centre, RMIT University

August 2014



Overview

We are honoured to make this submission in response to several queries raised in the Interim Report of the Inquiry in regard to International Engagement.

On the matter of international engagement, the FSI's Interim Report noted:

- Elements of Australia's financial system are internationally integrated, but a number of potential impediments have been identified
- Financial system development in the region will require continuing Government engagement to facilitate integration with Asia
- Government efforts to promote Australia's policy interests on international standard setting bodies have been successful
- Domestic regulatory processes could be improved to better consider international standard setting standards and foreign regulation, including processes for collaboration and consultation about implementation and mutual recognition and equivalence assessment processes
- Coordination of Australia's international financial integration could be improved, and FSI would value view on costs and benefits and trade-offs on – no change to current arrangements; amend the role of an existing co-ordination body to promote accountability and provide economy-wide advice to government

The Asia Pacific Financial Forum (APFF)

The Australian APEC Study Centre is involved in the work of the Asia Pacific Financial Forum (APFF). We supported the establishment of the APFF by helping organise a symposium on regional financial market integration in March 2012, a further symposium in Sydney in April 2013 which led to the agreement by APEC Finance Ministers to establish APFF. ABAC Australia was instrumental in the thinking to create APFF under the leadership of then-Chair of the APEC Financial System Advisory Group and ABAC Australia member, Mark Johnson AO.

At the heart of thinking behind the APFF are the following critical factors:

- The current heavy reliance on bank lending and the need to provide greater diversity in financial sources to effect regional economic transformation through the development of more efficient and liquid capital markets in some major regional economies
- The need for sound legal and regulatory frameworks to encourage market development
- Channelling regional savings through retirement and insurance schemes and their capital market activities into regional major investment needs, including importantly, infrastructure

- Regional financial integration to achieve economies of scale, greater depth and liquidity, and to enable market participants to become more efficient, innovative and competitive, as well as to increase consumer choice
- Recognition that governments and regulators in the region need to play a more active role in shaping financial regulatory standards and codes to ensure that standards contribute to regional development

More than 250 industry representatives/associations/academics have been involved in six major work-streams over recent months dealing with key issues identified at the Sydney Symposium to mobilise thinking on policy and regulatory reforms to respond to the critical factors outlined above. The output of the APFF is of very high quality, detailed and analytical. The major work-streams are:

- Lending infrastructure
- Trade and supply chain finance
- Capital markets
- Financial market infrastructure and cross-border practices
- Insurance and retirement incomes
- Linkages and structural issues.

The APFF convened a Forum in Seattle, USA in July 2014 to present and discuss the findings of an Interim Report on the work of the various APFF workstreams. The Interim Report will be delivered to APEC Finance Ministers, with the findings and proposed action plans to be discussed when Finance Ministers meet ABAC members in Beijing in October 2014. The Interim Report is attached to this submission as an additional document.

APFF recommends that it continues to serve as a regional platform for relevant participants from the public and private sectors, international and academic institutions to undertake, on a voluntary and self-funded or sponsorship basis a range of activities over the next two years. The activities include:

- The development of credit information sharing systems
- Proposals for reforms to improve the legal and institutional architecture for security interest creation, perfection and enforcement
- Promoting the use of moveable assets as collateral
- Workshops to enhance understanding of capital and liquidity standards, KYC, AML rules as they impact on trade and supply chains in the region
- Expanded use of electronic supply chain management platforms

- RMB Settlement with a focus on China and economies that form trade corridors with China
- Initiatives to develop classic repo markets and OTC derivative markets
- Support for the Asia Region Funds Passport – APFF has arranged a response to the consultative paper on the ARFP and will be involved in on-going work to promote and broaden participation
- Development of an enabling securities investment ecosystem to address cross-border market practices and domestic financial market infrastructure
- Workshops to help governments address demand and supply side issues in lifetime retirement income solutions and long-term investment activities of insurers
- Financial regulation in Asia focusing on financial supervisory structures, regional financial architecture, ARFP and Basel III, with work being undertaken by a Melbourne University research group
- Cross-border investment in Asia Pacific financial services and regional market connectivity

The Australian APEC Study Centre at RMIT University coordinates the work of the Linkages and Structures work-stream, and that work is reflected in the last two activities noted above.

Importantly, the public-private partnership approach reflected in the APFF is paying dividends. Making the reasonable assumption that Finance Ministers will welcome the recommendations in the Interim Report of the APFF the next phase should see close collaboration between members of the work-streams and financial system regulators in the region. Buy-in from regulators is a critical aspect of the process of reforming the region's financial markets. This will be important over the next two years, as the APFF intensifies its work and recommendations on developing solutions to the issues highlighted above.

The Interim Report of the APFF is available in the public domain and can be accessed [here](#).

APFF's work and suggestions for FSI's international integration focus

FSI notes that elements of the Australian financial system are internationally integrated. And so they are if judged in the context of the numbers and range of international financial groups operating in Australia and by Australian owned groups operating businesses in the region and globally. But, as demonstrated by the Asian Financial Crisis and later the GFC, the Asian region (and Australia itself) is vulnerable to external financial shocks. This is due, in part, but certainly not wholly, to the lack of a process in the region aimed at promoting closer regional financial market integration. The APFF is addressing the absence of such a process. That is of great relevance to Australia because Asia is increasingly important to Australia's real economy prospects.

A sustainable and stable long-term growth path for major Asian economies does require reforms to financial systems in those economies, and across the region, and it is in Australia's interests to support relevant and effective mechanisms that will help strengthen the region's finances. The APFF has the potential for being such a mechanism. It is inclusive, involves private and public sector groups of influence and it should be seen by Australia as a real means of helping shape valuable outcomes for regional economies (and for Australia).

By way of example, the Asia Region Funds Passport (ARPF) is beginning to gain momentum, and assuming it does become an important process for common issuance of collective securities in the region, it would enhance competition and improve efficiencies in the Australian market. It would do the same for other participating economies.

Collaboration on cross-border finance, mutual recognition and working with APFF workstreams on retirement income and long-term investment by pension funds and insurers are clearly as important to Australia's future role in the region as they are to other economies in Asia and the Pacific.

Deeper collaboration on ways in which to mobilise long-term savings for infrastructure financing for developing economies in the region would help promote sustainable growth in the region, and of course be of long-term benefit to Australia.

We propose that the FSI in its Final Report encourage Australia's regulators to play a prominent and active role in seeking the collaboration of counterpart regulators in the region in supporting the work of APFF. For regulators, this need not be, and should not be, at the expense of work in international standard setting bodies. But Australia's financial system regulators could play an influential role in encouraging other regulators in the region to participate in promoting regional financial system integration through APFF. FSI should also encourage more private sector finance groups to engage in the work of APFF.