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The evolving multilayered global financial safety net: The case of the Association of Southeast Asian Nations+3 regional financial safety net and the International Monetary Fund

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ADB Working Paper Series

**THE EVOLVING MULTILAYERED
GLOBAL FINANCIAL SAFETY NET:
THE CASE OF THE ASSOCIATION
OF SOUTHEAST ASIAN NATIONS+3
REGIONAL FINANCIAL SAFETY NET
AND THE INTERNATIONAL
MONETARY FUND**

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Abstract

This paper argues that in the aftermath of the global economic crisis, the centralized international monetary architecture or the global financial safety net (GFSN) set up at the Bretton Woods conference is evolving towards a more decentralized multilayered safety net comprising (i) the G20 at the apex as an overarching institution, (ii) multilateral financial safety nets (MFSNs) established under the auspices of the International Monetary Fund (IMF), (iii) bilateral financial safety nets (BFSNs) among central banks, (iv) regional financial safety nets (RFSNs) established in various regions of the world, and (v) national financial safety nets (NFSNs) or reserve accumulation by individual countries. The most significant factor explaining this evolution is financial globalization and the increased incidence of capital account crisis. As in many other regions of the world, Asia has established the ASEAN+3 RFSN, comprising the Chiang Mai Initiative Multilateralization (CMIM) and ASEAN+3 Macroeconomic Research Office (AMRO), for crisis prevention and management. The ASEAN+3 RFSN seeks to complement the IMF. However, because of its ad hoc nature and the relatively small size and cumbersome disbursement procedures, it is unlikely that this facility will be utilized when the next financial crisis hits the region. Based on Europe's experience with RFSN and IMF cooperation, the paper makes the case for a more structured form of cooperation between the ASEAN+3 RFSN and the IMF. Our proposal, together with the recent upgradation of AMRO to an international organization, could greatly enhance the effectiveness of the ASEAN+3 RFSN.

JEL Classification: F3, F33

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1. INTRODUCTION

The international monetary architecture or the global financial safety net (GFSN)¹ set up at Bretton Woods in 1944 was centralized, with the International Monetary Fund (IMF) being the sole multilateral institution to promote macroeconomic and financial stability by providing short-term financial support to countries facing a temporary balance of payments problem. Subsequently, the G7 was established in the mid-1970s to oversee the process of provision of public goods by various international economic institutions including the IMF. In the aftermath of the global economic crisis (GEC) of 2008–2009, this relatively centralized GFSN has evolved towards a more decentralized multilayered system comprising (i) the G20 at the apex as an overarching institution, (ii) multilateral financial safety nets (MFSNs) established under the auspices of the IMF, (iii) bilateral financial safety nets (BFSNs) among central banks, (iv) regional financial safety nets (RFSNs) established in various regions of the world, and (v) national financial safety nets (NFSNs) or reserve accumulation by individual countries. The most significant factor explaining this evolution is financial globalization and the increased incidence of capital account crisis – associated with large inflows and sudden reversals of capital flows and the bursting of asset bubbles. As Kawai and Rana (2009) have argued, preventing and managing such crises requires actions at the global, regional, and national levels.

The multilayered GFSN is still evolving and needs to be strengthened further to prevent a systemic crisis and protect innocent bystanders in the future. The relationship between institutions at different layers also needs to be spelled out. In particular, should RFSNs complement or compete with global institutions? This topic was introduced as a new agenda item at the Seoul G20 Summit of November 2010 where the leaders agreed that “Strengthened GFSNs can help countries to cope with financial volatility, reducing economic disruptions from sudden swings in capital flows and the perceived need for excessive reserves accumulation.” They also agreed to explore “ways to improve collaboration between regional financing arrangements and the IMF, acknowledging the potential synergies from such collaboration” (The G20 Seoul Summit Leaders Declaration 11–12 November 2010). The following year, in November 2011, the G20 leaders endorsed six broad principles for cooperation between RFSNs and the IMF (G20 2011).

The objectives of this paper are threefold: (i) to briefly review trends in the GFSN and the factors responsible for the developments; (ii) to outline the progress in the ASEAN+3 RFSN (namely, the Chiang Mai Initiative Multilateralization [CMIM] and ASEAN+3 Macroeconomic Research Office [AMRO]) and its relationship with the IMF; and (iii) to provide recommendations to strengthen the ASEAN+3 RFSN and its complementarity with the IMF. It is hoped that these recommendations, together with the recent upgradation of AMRO to an international organization, will ensure that the ASEAN+3 RFSN will be utilized the next time that a financial crisis hits the region.

¹ The GFSN refers to a set of crisis prevention and resolution instruments encompassing self-insurance (reserves), bilateral arrangements (swap lines between central banks), regional arrangements, and multilateral arrangements with the IMF in the center (<http://www/imsreform.org/safety>).

While several authors (e.g., Henning 2011a and Volz 2012) have argued that the relationship between the ASEAN+3 RFSN and the IMF should be cooperative and complementary, some others (e.g., Ocampo and Titelman 2012) have argued that RFSNs should be standalone and independent. The main hypothesis of this paper is that beyond a certain amount of “healthy” competition,² RFSNs should cooperate with and complement global institutions. This is for a number of reasons. First, both regional and global institutions have relative comparative advantages in different areas – cross-regional expertise and experience plus institutional memory in the case of the former, region-specific knowledge and proximity in the latter. Second, the demand for international public goods are sufficient for both to coexist. Third, managing financial globalization needs global, regional, and even national institutions (Kawai and Rana 2009). The paper, however, argues that the present ad hoc method of promoting complementarity between the ASEAN+3 RFSN and the IMF is not good enough. The small size of the funds available and possible delays in disbursement are also constraints. Based on the experience of Europe, we make the case for a more structured form of RFSN and IMF complementarity and argue that this modality of cooperation will enhance the effectiveness of the ASEAN+3 RFSN so that it could be utilized when the next financial crisis hits the region. Our proposal is mutually beneficial to both the ASEAN+3 RFSN and the IMF. The recently acquired international organization status by AMRO strengthens the case for our proposal because it gives AMRO the mandate to deepen its surveillance over the ASEAN+3 countries, either individually or collectively. AMRO should now be able to access confidential data about countries. It should also be able to field joint missions with the IMF,³ and its surveillance should be able to go beyond “peer review and peer pressure” to “due diligence.”⁴

A more structured form of cooperation with the IMF seems to be in the mind of the ASEAN+3 leaders as well. Their recent Joint Statement states: “We noted the completion of the CMIM studies on ‘Troika’s Financial Assistance Programs in the Euro Area for CMIM’s Future Reference’” (The Joint Statement 2016). The Statement also adds: “..we tasked the Deputies to carefully study how the CMIM can be better integrated into the global financial safety net. To this end, we welcomed a “test run” to be conducted this year on the crisis resolution facility linked to the IMF program.”

The paper is organized as follows: Section II outlines the move from a centralized GFSN set up at Bretton Woods to a multilayered GFSN. Section III discusses the reasons for the change. It argues that among the various components of the GFSN, RFSNs show the most promise and potential. But as noted by the G20, RFSNs should complement MFSNs and not try to supplant them. Section IV focuses on the development of the ASEAN+3 RFSN and explains why it was not utilized when the GEC affected the region in 2008. Section V examines the relationship between the European RFSN and the IMF and argues that, for various reasons, the ASEAN+3 RFSN should establish a more structured form of cooperation with the IMF in order to enhance their effectiveness. Section VI concludes.

² “Healthy” competition refers to competition that leads to reforms of institutions and increases in the supply of public goods, while unhealthy competition means a race to the bottom and implementation of “beggar thy neighbor” policies. The establishment of AMRO has led the IMF to produce regional outlook reports for Asia, for example.

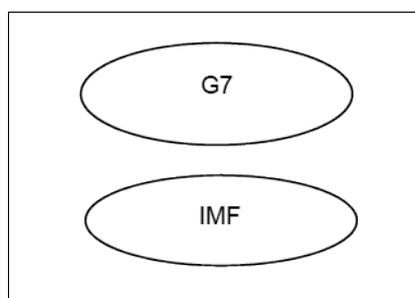
³ The author has been informed that, so the IMF does not welcome AMRO staff in its surveillance, AMRO staff are welcome only in the IMF’s routine economic review missions.

⁴ “Due diligence” involves a rigorous scrutiny of a potential debtor’s economy and policies from a potential creditor’s perspective (Kawai and Houser 2008).

2. FROM A CENTRALIZED TO A DECENTRALIZED GLOBAL FINANCIAL SAFETY NET

The GFSN that prevailed in the 1970s and 1980s is depicted in Figure 1. It comprised the IMF with the G7 as the oversight body. This architecture worked fairly well in promoting macroeconomic and financial stability aside from the Latin American debt crisis of the 1980s and the problems with the European Monetary System in the early 1990s.

Figure 1: Centralized Global Financial Safety Net of the 1970s and the 1980s



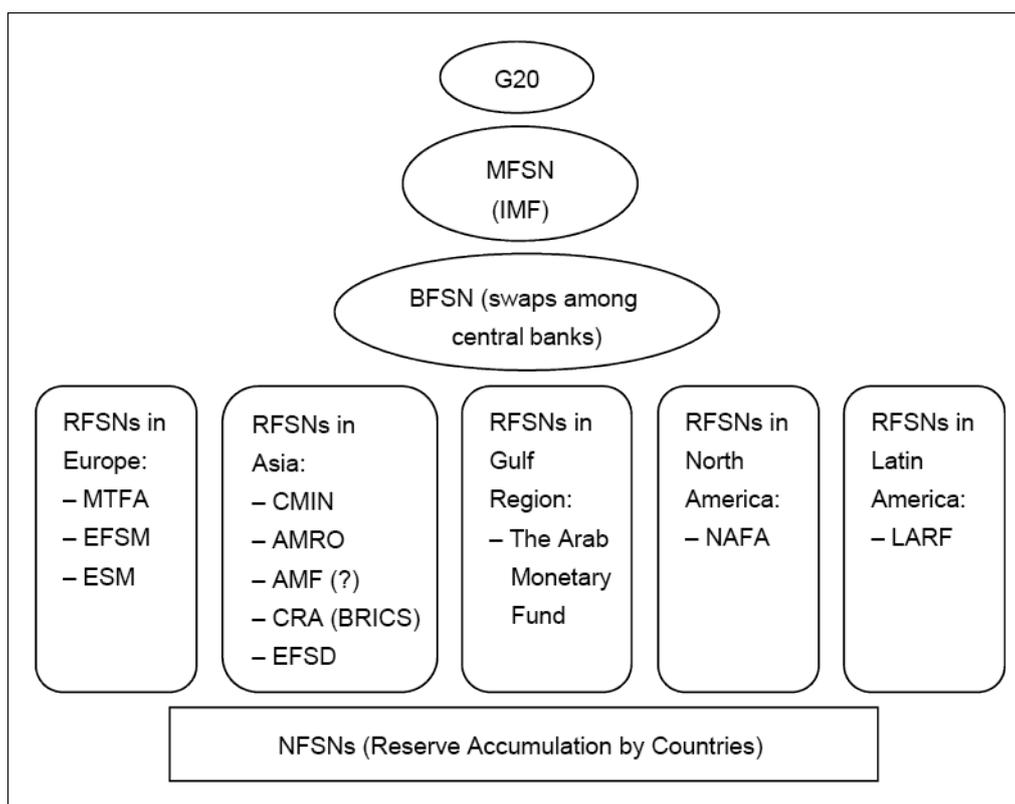
G7 = Group of Seven, IMF = International Monetary Fund.

In the aftermath of the global economic crisis, however, the centralized GFSN of the 1970s and 1980s is moving towards a more decentralized one comprising (i) the G20 as an apex body, (ii) multilateral financial safety nets (MFSNs) established under the auspices of the IMF, (iii) bilateral financial safety nets among central banks (BFSNs), (iv) regional financial safety nets (RFSNs) established in various regions of the world, and (v) national financial safety nets (NFSNs) or reserve accumulation by individual countries. The present GFSN is depicted in Figure 2.

The G20 is at the apex of the multilayered GFSN. The G20 Summit was established after the GEC by upgrading the G20 finance and central bank officials' forum, which started in 1999 but which was kept under the shadow of the G7. The leaders have self-appointed the forum as the "premier forum for international economic cooperation" including monetary cooperation. As already mentioned, since the Seoul Summit, the G20 has adopted the topic of strengthening the GFSN as one of its agenda items.

Following the London G20 Summit and the eurozone sovereign debt crisis, IMF resources have been substantially increased. Also, in an attempt to prevent and more effectively manage a capital account crisis, the IMF has revamped its lending policies. These include the various contingent financing facilities or MFSNs that have been established. In 2009, the IMF introduced a new Flexible Credit Line (FCL) designed to meet the increased demand for crisis prevention and crisis mitigation lending from countries with robust policy frameworks and very strong track records in economic performance. A year later it also introduced the Precautionary Credit Line (PCL) for countries with a sound policy track record and fundamentals that may not meet the FCL requirement. Proposals for a Global Stabilization Mechanism, where the IMF would finance a number of countries simultaneously, have also been launched, although it has not received enough support from member countries.

Figure 2: Multilayered Global Financial Safety Nets



AMF = Asian Monetary Fund; AMRO = ASEAN+3 Macroeconomic Research Office; BFSN = Bilateral Financial Safety Net; CMIM = Chiang Mai Initiative Multilateralization; CRA = BRICS Contingent Reserve Arrangement; EFSD = Eurasian Fund for Stabilization and Development; EFSF = European Financial Stability Facility; EFSM = European Financial Stabilization Mechanism; ESM = European Stability Mechanism; FLAR = Latin American Reserve Fund; NAFA = North American Framework Agreement.

Despite these innovations, the IMF’s capacity to prevent a crisis in the future is in doubt. The IMF’s FCL, which provides large-scale access to finance without conditionality to protect countries against contagion, has been taken up by only three countries (Colombia, Mexico, and Poland). Similarly, the PCL has been taken up by only one country (Macedonia). Stigma is a major problem – countries fear that applying for these facilities would be seen by capital markets as a sign of underlying weakness and as indicating that the countries were in difficulties. There is now talk of the IMF unilaterally prequalifying countries and of countries applying as a group so that no one country is singled out as a weak country.

In 2008, when countries faced a severe credit crunch because of the crisis in the US, the Fed extended \$30 billion in the form of bilateral swaps to Brazil, Mexico, Singapore, and the Republic of Korea. The Republic of Korea also obtained such funding from the Bank of Japan and the People’s Bank of China. Although some countries wish to establish BFSNs by regularizing these bilateral dollar swap arrangements entered into with various central banks in times of crisis, it may not be possible. For example, the swaps were criticized by the US Congress as giveaways to countries that could lead to moral hazard.

Efforts have also been made to establish or expand existing regional financial safety nets (RFSNs).⁵ Europe has the Medium-term Financial Assistance established in 1971 to support European Union (EU) members facing payment difficulties. In 1999, this program was narrowed to cover only the non-eurozone members. Subsequently, fears that the contagion from Greece could affect other countries in Europe led to the establishment in May 2010 of the European Financial Stability Facility (EFSF) for eurozone members and the European Financial Stabilization Mechanism (EFSM) for the all EU members. In 2012, the European leaders agreed to a permanent replacement of the EFSF by the European Stability Mechanism (ESM). The ESM is in effect a European monetary fund (Henning 2011a).

In 1994, the North American Framework Agreement (NAFA) was established as a parallel financing agreement to the North American Free Trade Agreement. Also, the Arab Monetary Fund was established in 1976, and the Latin American Reserve Fund in 1978.

In Asia, we have the CMIM and AMRO (discussed in Section IV). More recently, a few other RFSNs have been established. These include the contingent reserve arrangement (CRA) set up by the BRICS, and the Eurasian Fund for Stabilization and Development (EFSD) set up by Russia and the Central Asian Republics.

Data in Table 1 show that European RFSNs are the strongest in terms of financing capacity, speed of decision-making, impartiality, and the ability to work with the IMF. The Arab Monetary Fund and the Latin American Reserve Fund are older but have limited resources. Their surveillance capacity is fairly strong and they have no links with the IMF. The CMIM is in between with \$240 billion and is linked with the IMF. The surveillance capacity for the CMIM is also being built at the AMRO.

Many developing countries have built up foreign exchange reserves as first lines of defense. Pretty much every country that has been able to do so has accumulated ever-growing amounts of reserves intended to serve as self-insurance and thus prevent the need to resort to the IMF. While there is evidence that countries with more reserves did better during crises, self-insurance has its costs (Eichengreen 2010). Yields on reserve assets are low and accounting losses could be experienced if the country's currency appreciates vis-à-vis the dollar and euro. Further, reserve accumulation could aggravate the global imbalance problem.

3. FACTORS RESPONSIBLE FOR MULTILAYERED GLOBAL FINANCIAL SAFETY NET

The first and foremost factor responsible for the move towards a multilayered GFSN is the financial globalization of the post-1990 period. While policymakers had been wary of uncontrolled financial flows during the Bretton Woods era and in fact permitted capital controls, in the 1980s and 1990s under the Washington Consensus they embraced financial liberalization and deregulation, thereby ushering in an age of highly integrated financial markets and capital flows that have dwarfed the operation of the IMF. As early as the 1960s, the British had been promoting financial globalization through their support of deregulated Euromarkets for London. But the momentum accelerated when Thatcher in 1979 and Reagan in 1980 took political office. IMF management even launched an initiative in 1995 to overturn the commitment to capital controls by amending their articles of agreement in order to gain a liberalization

⁵ See McKay, Volz, and Wolfinger (2010) and Eichengreen (2010) for a comparative analysis of various RFSNs.

mandate with respect to capital movement. It was only recently that this initiative was withdrawn.

Table 1: Details of Regional Financial Safety Nets

	Europe	Chiang Mai Initiative Multilateralization (CMIM)
Brief Description	<ol style="list-style-type: none"> 1. Medium-Term Financial Assistance (MTFA) established in 1971 to provide financial support to all EU members facing payment difficulties: since 1999 covers only non-eurozone members. 2. The European Financial Stability Mechanism (EFSM) was established in May 2010 with similar mandate to MTFA but covers all EU members. 3. The European Financial Stabilization Facility (EFSF) was established in May 2010 and covers only eurozone countries. In 2012, the EFSF evolved into the European Stability Mechanism (ESM). 	The Chiang Mai Initiative of May 2000 became the CMIM or a “self-managed” reserve pool of \$120 billion in March 2010. Two years later the size of the pool was doubled to \$240 billion.
Adequacy of finance	MTFA: Max. capacity presently €50 billion EFSM: €60 billion ESM: €500 billion	\$240 billion
Surveillance capacity	Decisions are taken by the Economic and Financial Affairs Council based on the recommendations of the Commission or request of a member: strong surveillance.	The ASEAN+3 Macroeconomic Research Office (AMRO) was established in May 2011 in Singapore as an independent surveillance unit. AMRO’s purposes are to (i) monitor and analyze regional economies and (ii) contribute to (a) an early detection of risks, (b) policy advice for remedial actions, and (c) effective decision-making of the CMIM. AMRO became an international organization on 9 February 2016.
Speed of decision-making	Relatively fast	Procedures established but could be slow
Impartiality in lending decisions	Impartial	Impartial
Ability to work with IMF	Working closely with the International Monetary Fund (IMF) in resolving the present eurozone crisis	Withdrawal beyond the delinked portion linked to an IMF program
	The Arab Monetary Fund	The Latin American Reserve Fund (FLAR)
Brief Description	The Arab Monetary Fund started operations in 1977. It has 22 member countries and has provided 146 loans benefiting 14 countries.	It was established in 1978. Membership comprises 5 Andean countries and Uruguay. Originally it focused on providing balance of payments support. Now it also helps with debt restructuring and harmonizing macroeconomic policies of members.
Adequacy of finance	Its paid-up capital is small, only \$3 billion.	It has roughly \$2 billion of paid-up capital. FLAR can borrow specified amounts.
Surveillance capacity	It has a technical staff of 50 and conducts regular country reviews.	FLAR has an Economic Studies Department and is quite effective.
Speed of decision-making	Relatively fast	Relatively fast
Impartiality in lending decisions	Impartial	Impartial
Ability to work with IMF	No provision for working with the IMF	No provision for working with the IMF

Sources: Data from McKay, Volz, and Wolfinger 2010; Eichengreen 2010; Park 2011; and others.

With financial globalization not only has the incidence of financial crisis increased⁶ but its nature has also changed. The crises of the past were currency crises or debt crises due mainly to governments borrowing excessively in international capital markets to finance their current account deficits. Speculative attacks occurred as the international reserves of the country fell below a critical level. These were the standard currency crisis or the “generation one”-type crisis first discussed by Krugman (1970).

With financial globalization, a new type of crisis called “capital account crisis” or “generation three” crisis (Dornbusch 2001) – associated with large inflows and sudden reversals of capital flows and the bursting of asset bubbles and a banking crisis – have started to hit emerging markets.⁷ Such crises tend to affect the balance sheets of countries and solvency positions. The costs of balance sheet recessions tend to be higher and recovery from the crisis also takes a longer time. They also tend to be systemic, affecting most or all sectors of the economy with strong contagion to neighboring countries (which may be innocent bystanders).

Based on the experience with the Asian financial crisis, Kawai and Rana (2009) had argued that efforts to prevent and manage a capital account crisis required actions at the global, regional, and national levels. Last year, the G20 came up with a similar message in relation to the global economic crisis: “Current volatility of capital flows is reflecting the differing speed of recovery between advanced and emerging market economies. National, regional, and multilateral responses are required” (G20 Seoul Summit Leaders Statement). The IMF had until recently not appreciated the value of RFSNs. But now that view is changing and the IMF is working closely with various FSFNs (especially those in Europe in attempting to resolve the eurozone crisis. In 2010, the IMF organized a high-level seminar to create stronger links with RFSNs (Goretti, Lanua, and Ramakrishnan 2010). There is, therefore, a consensus now that we need a multilayered GSFN and global and regional policy coordination. Regional policy coordination could add value in two ways. First, policymakers tend to be more frank when discussing policies with neighboring countries than at the global level. Second, a regional policy agenda also tends to be more focused on the common issues affecting a set of countries rather than those at the global level.

Second, the governance system of the international monetary architecture in the 1970s and the 1980s reflected the dominance of the US and this system lacked legitimacy and needed to be changed in an environment where the economic and political power of emerging markets, particularly those in Asia (the PRC and India), was rising rapidly. Emerging markets whose footprint in the global economy is increasing rapidly must also participate in global governance.

According to the long-term projections made by Goldman Sachs, emerging markets will continue to grow rapidly over the next 40 years. In 2003, Wilson and Purushothaman (2003) projected that the three largest economies in the world by 2050 would be the PRC, the US, and India. In 2007, Poddar and Yi (2007) revised this ranking to the PRC, India, and the US. More recently, the Kohli and Sood (2010) projected that the above ranking could be obtained even earlier, within the next 30 years. Despite their economic dynamism, the PRC and India will be very much behind the US in terms of per capita incomes, poverty, and military might.

⁶ Kawai and Rana (2009) noted that 10 such crises had hit countries all over the world since the Asian financial crisis of 1997–1998. Chamon, Ghosh, and Kim (2010) identified more episodes of such crisis.

⁷ “Generation two” crises are the self-fulfilling type of crisis that hit the European Monetary System in 1992/1993.

Third, the IMF is a club in the sense that it produces a benefit that is partially nonrivalrous (more than one user can consume) and at least partially excludable (users can be denied access to them). Kawai, Petri, and Sisli-Ciamarra (2009) applied the theory of clubs to explain that the IMF, like other clubs, is an inflexible institution designed to maintain firm control in the hands of the founding members and not be open to allowing new members into its governance system. The charter, quotas, and voting rights of the IMF were designed in the interest of like-minded original core members in 1944 and placed strict limits on change as membership expanded. That is why even though the G20 has pledged to allocate higher quotas and voting power to emerging markets, governance reform of the IMF can only proceed at a glacial pace.⁸ In comparison with the 44 countries that participated at the Bretton Woods conference, the membership of the IMF now stands at 187.

Kawai, Petri, and Sisli-Ciamarra (2009) examined the evolution of the shares of developing and emerging markets in IMF quotas, and in global trade and GDP (in terms of purchasing power), two rough indicators of their importance in the world economy. They found that the trade shares of developing and emerging economies have risen more rapidly than their share in IMF quotas. This contrast is even clearer for their share of world GDP. Quotas, which also determine voting power at the IMF, are especially low for the rapidly growing emerging market countries, such as Brazil, the PRC, and India. Kelkar et al. (2005) found that these three countries had 19% fewer votes than Belgium, Italy, and the Netherlands collectively, although they had 21% more nominal GDP, 400% more purchasing power GDP, and 2,800% more population in the second group. On the other hand, Europe controls, directly or indirectly, 10 chairs out of 24 on the IMF Board even though it has a common monetary policy and it has 30% of quota and voting rights.

Fourth, another reason why Asian countries have adopted national and regional self-help measures is to protect themselves from the policy mistakes made by the IMF in managing the Asian financial crisis. The IMF saw the Asian financial crisis as a standard current account crisis and recommended its standard prescription to manage it, comprising tighter monetary and fiscal policies and a currency crisis. These policies aggravated the impacts of the capital account crisis where an appropriate response would have been to pump liquidity into the system through expansionary monetary and fiscal policies – just the opposite of the policies that the IMF prescribed. The IMF also prescribed too many structural conditions that extended beyond its core competencies.⁹

The fifth is an argument for competition, particularly in the supply of services to small and medium-sized countries. Owing to their small size, the power of these countries to negotiate with large organizations is limited, and their most important defense is therefore competition in the provision of financial services to them (Ocampo 2010).

⁸ The 2010 IMF Governance Reform Bill was finally approved by the US Congress in December 2015. But it is regarded as “too little, too late” and “two steps forward, one step back” by many analysts.

⁹ An IMF Independent Evaluation Office (2003) report accepts many but not all of these criticisms. More recently, Ostrey, Lougani, and Furceri (2016) concluded that “instead of delivering growth, neoliberal policies have increased inequality, in turn jeopardizing durable expansion.” The policies called into question are unfettered flows of hot money, and excessively rapid efforts to reduce public debt.

The final argument relates to the fact that regional and subregional institutions enjoy a greater sense of ownership because member states, particularly small ones, feel that they have a strong voice in these organizations. The “preferred creditor status” that results from this fact reduces the risks that regional reserve funds face, further encouraging the virtues of risk pooling (Ocampo 2010). Large regional countries may be willing to take a lead role in regional bodies before global bodies.

4. ASEAN+3 REGIONAL FINANCIAL SAFETY NET AND COMPLEMENTARITY WITH THE INTERNATIONAL MONETARY FUND

Before the Asian Financial Crisis (AFC) of 1997–1998, the only RFSN in Southeast Asia was the ASEAN swap arrangement (ASA), which was established in August 1997 when the original members of ASEAN – Indonesia, Malaysia, the Philippines, Singapore, and Thailand – agreed to a reciprocal currency swap arrangement among themselves. The idea was to provide liquidity support to members experiencing balance of payments difficulties. The maximum amount of liquidity available under the ASA was \$100 million, with each member providing \$20 million. Subsequently, the maximum amount was doubled to \$200 million. The size of the ASA was too small to be of use in helping countries manage the AFC and so it was not used.

The AFC led countries to revisit the issue of an RFSN mainly because of the way in which the IMF managed the crisis. Four of the crisis-affected countries – Indonesia, the Republic of Korea, the Philippines, and Thailand – had accepted an IMF program, while Malaysia went alone. The IMF misdiagnosed the problem and prescribed the wrong medicine – a fact that it acknowledged later (e.g., Sussangkarn 2010). It was also believed at the time that the IMF might not have adequate resources to help countries manage a “capital account” crisis associated with large inflows and sudden reversals of private capital flows (e.g., Kawai and Rana 2009).

There were calls to establish the Asian Monetary Fund, which did not materialize because of insufficient support within the region and predictable opposition from the US. Nevertheless, there was a strong feeling among policymakers that a regional financing facility in the region could act as the first line of defense by providing short-term liquidity and thereby preventing a crisis when speculative attacks occur (e.g., Sussangkarn 2010). Therefore, at their May 2000 meeting in Chiang Mai, the ASEAN+3 finance ministers agreed to launch the Chiang Mai Initiative (CMI) as a regional “self-help and support mechanism” to provide “sufficient and timely financial support to ensure financial stability in the East Asia region” (The Joint Statement 2000). The CMI expanded the ASA to all ASEAN members and set up a network of bilateral swaps among the ASEAN+3 countries. The ASA was subsequently expanded to \$100 billion and then to \$200 billion in April 2005. ASEAN+3 countries also signed bilateral swaps among each other and by 2008 there were 16 bilateral swaps amounting to \$84 billion.

Pursuit of complementarity has been the key focus of the ASEAN+3 RFSN. In their May 2000 Joint Statement, the ASEAN+3 Finance Ministers had stipulated that the RFSN in East Asia should “supplement the existing international facilities,” and the way that complementarity was promoted in the CMIM (and its predecessor, the CMI) was by requiring the existence of an IMF-supported program to provide assistance in excess of a certain percentage of maximum access. Initially, only 10% of the maximum access was readily available with 90% being linked to an IMF program. The size of the

delinked portion was subsequently increased. The link to the IMF was also intended to address the moral hazard problem in lending and the lack of independent surveillance capacity in the CMI. By 2008, the ASEAN+3 countries had signed 16 bilateral swaps among each other amounting to a total of \$86 billion.

In the aftermath of the severe credit crunch that the region experienced because of the GEC in 2008, the CMI bilateral swaps were not used. This was because of the small size of the swaps (including the delinked portions)¹⁰ and the absence of a rapid response mechanism to trigger the swaps (each bilateral swap had to be triggered one at a time).

Since then, ASEAN+3 has taken a number of actions to increase the financial resources available from its RFSN and to clarify the disbursement procedures. These include doubling the size of the CMIM, increasing the delinked portion to 30% with a view to increasing it further to 40% subject to review, and agreeing to the decision-making process and operational guidelines (Box 1). AMRO also now has the status of an international organization. This means that AMRO is no longer a business entity subject to rules and regulations of Singapore, where it is housed, but an ASEAN+3 institution with a mandate for surveillance of the member countries either individually or collectively. Are these actions sufficient to ensure that the CMIM will be utilized when the region faces the next crisis? Probably not.

Under the new agreement, five ASEAN members (Indonesia, Malaysia, the Philippines, Singapore, and Thailand) can borrow a maximum amount of approximately \$23 billion each from the CMIM with an IMF program in place – one third of which will be the delinked portion – under a single contract at one go (Hill and Menon 2014).¹¹ These amounts are large compared to the old CMI swaps, but still inadequate to prevent and manage the newer types of capital account crisis associated with large inflows and sudden withdrawal of short-term financial capital.¹² It is unlikely that ASEAN+3 countries will increase their commitments to the CMIM and increase the percentage of the delinked portion without the capacity of AMRO being strengthened significantly for regional surveillance and for designing conditions under which funds can be loaned out (otherwise there could be moral hazard). Although AMRO has come a long way, as a relatively new institution it still lacks the research capacity, human resources, and experience to serve as an “independent surveillance unit” for the CMIM.

More important is the speed and efficiency with which requests for assistance can be disbursed (Hill and Menon 2014). The operational guidelines for the CMIM note that a decision based on a two thirds majority is to be made within two weeks of the swap request. This is unlikely to happen as the CMIM is not a centralized fund, but a “self-managed” arrangement where contributions are held by individual central banks and monetary authorities. Also, the decision rests with a nonresident body and there is uncertainty regarding the nature of the information and analysis required to facilitate the decision-making. In contrast, bilateral swaps with the advanced countries are fast-disbursing and come without explicit conditionalities as they are well collateralized.

¹⁰ For example, the Philippines and Thailand had two swaps each with Japan and the Republic of Korea for \$2.5 billion and \$4 billion, respectively.

¹¹ The Republic of Korea and Japan are entitled to borrow a maximum of \$38.4 billion for the CMIM with an IMF program in place. The PRC can borrow about \$35 billion, Viet Nam \$10 billion, and Cambodia, the Lao People’s Democratic Republic, and Myanmar about \$1 billion.

¹² The economic and social costs and the contagion effects of a capital account crisis tend to be high. During the recent eurozone crisis, two separate packages of \$142 billion and \$130 (in today’s dollars) were put together for Greece and \$100 billion for Portugal.

5. PROPOSAL FOR STRUCTURED ASEAN+3 REGIONAL FINANCIAL SAFETY NET AND INTERNATIONAL MONETARY FUND COOPERATION

ASEAN+3 and the IMF, therefore, need to move beyond ad hoc collaboration to develop a more structured form of cooperation by pooling financial, human, and technical resources. An example worth considering is the IMF's cooperation with various European RFSNs¹³ to resolve the eurozone crisis. In Europe, countries that are members of both the EU and the IMF request financial assistance simultaneously from the two institutions. In the case of assistance to EU members outside of the eurozone, discussions are conducted jointly with the government authorities, the European Commission (EC), and the IMF (Table 2). In addition, the European Central Bank (ECB) participates in the discussions when the borrowing country is in the Eurozone, forming the "Troika" framework between the IMF, EC, and ECB. In designing policies and conditionalities, there is a clear division of labor with the IMF focusing on the macroeconomic framework, the EC ensuring that the conditionality is consistent with EU-wide rules and institutions particularly with the fiscal targets, and the ECB ensuring that the financial sector strategy is sufficiently robust. The "Troika" members discuss the program among themselves before presenting it to the authorities. Two separate program documents are prepared, one for the IMF board and another for the EC. Programs are co-financed with no single rule for burden sharing between the IMF and European RFSNs. In Latvia in 2008 and Greece in 2012, the IMF provided about 20% of the total financing while European RFSNs provided the balance. On the other hand, in Hungary in 2008 and Romania in 2009/2011, the IMF provided over 60% of the financing.

The IMF's assessment of this cooperation is that although the difference of views among institutions continues to pose a challenge, "On the ground, the Troika structure has enabled effective information sharing, more streamlined program discussions and reviews, and helped ensure that external communications are well coordinated" (IMF 2013, 22). The recent IEO report (IEO 2016) highlighting the IMF's lending to Greece and Ireland in 2010 and Portugal in 2011 also finds that the Troika arrangement proved to be an efficient mechanism in most instances, "but the IMF lost its characteristic agility as a crisis manager." This happened "because the European Commission negotiated on behalf of the Eurogroup" and "subjected the IMF's technical judgement to political pressure from an early stage." The report mentions that the "IMF treated Europe differently" and that "it was easily swayed by European officials." The report mentions that the Fund failed to "play its customary sole and lead role" that it adopts when lending to developing countries. Instead the IEO argues that the IMF's Troika partners had "veto power" over the Fund.

¹³ The European Financial Stabilization Mechanism (which provides balance of payments support to all EU members) and the European Stability Mechanism (which safeguards against financial crisis in the eurozone countries).

Table 2: The International Monetary Fund's Engagement with European Partners

	EU member (not in the eurozone)	Eurozone member
Partners	Authorities + European Commission (EC) + International Monetary Fund (IMF)	Authorities + Troika (ECB + EC + IMF)
Program Document	Memorandum of Economic and Financial Policies for IMF Board and Memorandum of Understanding for EC	Memorandum of Economic and Financial Policies for IMF Board and Memorandum of Understanding for EC
European RFSN	European Financial Stabilization Mechanism (EFSM) for balance of payments assistance	European Financial Stabilization Mechanism (EFSM) for balance of payments assistance European Stability Mechanism for financial stability
Designing of Policies	IMF: macroeconomic framework EC: ensuring consistency with European Union (EU)-wide rules particularly on fiscal targets	IMF: macroeconomic framework EC: ensuring consistency with EU-wide rules particularly on fiscal targets ECB: financial sector strategy
Co-financing between IMF and European RFSNs	Programs are co-financed between the two with no single rule for burden sharing	Programs are co-financed between the two with no single rule for burden sharing

Source: IMF. 2013. "Stocktaking the Fund's Engagement with Regional Financial Arrangements." 11 April.

Since the present modality of cooperation between the ASEAN+3 RFSN and the IMF is unlikely to be successful, a more structured form of cooperation between the two institutions should be considered. This framework would involve pooling of financial, human, and technical resources between the ASEAN+3 RFSN and the IMF in three cooperative activities (Table 3).

Table 3: Structured ASEAN+3 Regional Financial Safety Net and International Monetary Fund Collaboration

Our Proposal	Advantages
CRISIS MANAGEMENT Simultaneous request for financial assistance from CMIM and IMF and joint analysis and evaluation	<ul style="list-style-type: none"> – Bring in expertise from outside East Asia to supplement AMRO resources – IMF staff, in theory, would be more dispassionate to regional countries – Overcome IMF "stigma"
Joint monitoring and surveillance, joint AMRO-IMF missions, and jointly developed conditionality	<ul style="list-style-type: none"> – Focus on relative comparative advantages (IMF, macro and macro financial and cross-regional experience: AMRO, regional financial and capital market developments, and structural reforms)
Co-financing (with amounts depending on country-specific basis) and joint supervision	<ul style="list-style-type: none"> – Would leverage CMIM funds as IMF funds would also come in
CRISIS PREVENTION Joint assessment (of eligibility) and co-financing	<ul style="list-style-type: none"> – Focus on relative comparative advantages – Would leverage CMIM funds as IMF funds would also come in

AMRO = ASEAN+3 Macroeconomic Research Office, CMIM = Chiang Mai Initiative Multilateralization, IMF = International Monetary Fund.

Source: Author

First, as in Europe, ASEAN+3 countries seeking financial resources should be required to apply simultaneously to both the IMF and CMIM and the IMF and AMRO should jointly analyze and evaluate the applications. Currently, the analysis and evaluation by the two institutions are separate with AMRO responsible for CMIM funds. But AMRO's capacity is limited and it will take a long time to strengthen it. Involving both the IMF and AMRO in the analysis and evaluation process would increase its robustness in two ways. Firstly, experts from outside East Asia would support an understaffed AMRO, which would nonetheless arguably be less politicized than any CMIM members meeting. Decisions on applications could therefore be made more rapidly and involving IMF staff who, at least in theory, should feel more dispassionate about the country requesting a CMIM package. A crisis triggering an application for CMIM funds would need a decision to be taken in the shortest period of time and with the smallest moral hazard possible. IMF and AMRO intervention in the decision-making process would help both.

In addition, joint application to both the IMF and CMIM would help address the IMF stigma in East Asia. Given the experience of Indonesia, the Republic of Korea, and Thailand during the 1997 AFC, politically it would be very difficult to sell an IMF program anywhere in East Asia. Having a joint process together with an ASEAN+3 institution (AMRO) would eliminate such a stigma.

The second area of cooperation between ASEAN+3 and the IMF would be in the area of joint monitoring and surveillance, joint missions, and joint conditionality. Given that the IMF and AMRO analyses have the common goal of ensuring that signs of financial vulnerability are caught well on time to prevent a possible crisis, it would make sense for the two institutions to pool their capabilities. The two institutions should focus on their relative comparative advantages – the IMF on macro and micro financial and cross-regional experience and AMRO on regional financial and capital market developments and structural reforms.

AMRO staff are from ASEAN+3 countries, giving them familiarity with one or more countries in the region – including relevant language skills and cultural understanding. For its part, the IMF is better resourced and has staff with knowledge about macro and financial systems in different parts of the world. Pooling their resources together through joint IMF-AMRO missions and analysis including joint conditionality would strengthen the surveillance mechanism.

The third area of cooperation would be co-financing and joint supervision of liquidity provision programs. Currently, financing would only come from the CMIM pool, which, as already explained above, would probably be insufficient to avert the spread of a financial crisis. Co-financing with the IMF would substantially increase the resources available for ASEAN+3 to deal with a financial crisis. As the experience of joint EU-IMF programs shows, the percentage of a total rescue package coming from the RFSN and the IMF can be negotiated on a case-by-case basis. Also, joint supervision of any approved liquidity provision program would be the natural consequence of joint approval and financing.

6. CONCLUSIONS

In the future, the decentralization of the GFSN is expected to continue. The incidence of capital account crisis is also expected to increase. The existing ASEAN+3 RFSN is, however, unlikely to be successful in crisis prevention and management. This is because of the present ad hoc modality of cooperation between the ASEAN+3 RFSN and the IMF, the relatively small size of the funding available, and the cumbersome

disbursement procedures. Therefore, a more structured form of cooperation between the two institutions should be considered as in Europe. This framework should involve pooling of financial and technical resources between the ASEAN+3 RFSN and the IMF in three cooperative areas: (i) joint AMRO-IMF analysis and evaluation of all applications for CMIM liquidity, (ii) joint surveillance, joint AMRO-IMF missions, and jointly developed conditionality, and (iii) co-financing of programmes by the ASEAN+3 RFSN and the IMF, with the amounts determined on a country-specific basis, and joint supervision. Our proposal for a more structured cooperation between the ASEAN+3 RFSN and the IMF, together with the recently upgraded status of AMRO, which strengthens its surveillance capacity, should lead to an effective regional safety net in Asia.

The timing is also appropriate for a more structured form of complementarity between the ASEAN+3 RFSN and the IMF for two reasons. First, after the AFC, countries in the region had the IMF stigma that originated from the feeling of being unfairly treated and being forced to accept inappropriate conditions. This is now changing and the IMF is invited to the surveillance meetings of the ASEAN+3 ministers together with AMRO. The IMF has also engaged in dialogues with AMRO as part of its outreach activities, although it does not have a formal technical assistance program with it. This engagement should be deepened further to a more structured form of ASEAN+3-IMF cooperation as outlined above. Second, AMRO is now an international organization that has a mandate from the ASEAN+3 countries to conduct policy dialogues and surveillance of member countries either individually or collectively. The IMF should, therefore, invite AMRO staff to join its crisis management missions and seek their views and inputs in designing conditionality.

Box 1: Actions taken to Strengthen the ASEAN+3 Regional Financial Safety Net since the Global Economic Crisis

- (i) The CMI has been multilateralized into the Chiang Mai Initiative Multilateralization (CMIM).

In March 2010, the bilateral swaps were combined and expanded to become the CMIM, a \$120 billion “self-managed reserve pool” governed by a single contract. As a self-managed reserve pool, the contributions remain in the central banks of the member countries and are not actually paid into a centralized reserve pool. Two years later the size of the pool was doubled to \$240 billion.

- (ii) Contributions, borrowing rights, and operational guidelines of the CMIM have been fixed.

All ASEAN+3 member countries (plus Hong Kong, China) have contributed to the CMIM and are eligible to borrow from it using a multiplier (so that the smaller countries can borrow more) in case they face a payment problem. To access the CMIM, a member country must submit a request to the Coordinating Countries (the co-chairs of the ASEAN+3), which then deliver the request to a nonresident Executive-Level Decision-Making Body. This body then has to convene and make a decision based on a two thirds majority within 2 weeks from the receipt of the swap request.

continued on next page

- (iii) The ASEAN+3 Macroeconomic Research Office (AMRO) has been established and its capacity is being enhanced.

With the multilateralization of the CMI, there was a need for an independent surveillance unit to conduct due diligence so that the borrowing countries' capacity to repay the loan could be assessed. In May 2011, the AMRO was established as a limited company in Singapore. AMRO's activities are divided into functions during so-called peace time and crisis time. During peace or noncrisis periods, AMRO's main responsibility is to prepare quarterly consolidated reports on the overall macroeconomic assessment of the ASEAN+3 region as well as on individual ASEAN+3 countries. Should a crisis occur, however, its role and responsibilities multiply. During crisis time, AMRO is tasked to:

- (a) provide an analysis of the economic and financial situation of the CMIM Swap Requesting Country;
- (b) monitor the use and impact of the funds disbursed under the CMIM Agreement;
- (c) monitor the compliance by the CMIM Swap Requesting Country with any lending covenants to the CMIM Agreement.

AMRO is governed by an executive committee comprising the deputy Finance Ministers and deputy central bank governors of the ASEAN+3 countries. At present, AMRO is being run by a small staff complement of about a dozen led by the AMRO Director.

- (iv) Several other decisions were taken at the May 2012 meeting of the ASEAN+3 Finance Ministers:
- (a) The delinked portion was increased to 30% with a view to increasing to 40% subject to review.
 - (b) The ASEAN+3 Finance Ministers Meeting was upgraded to the ASEAN+3 Finance Ministers and Central Bank Governors Meeting. For the first time, the central bank governors of the 13 countries plus the head of the Hong Kong Monetary Authority were invited to participate in the forum. This was a significant move as it brought together officials handling tax/expenditure policies with those handling monetary and exchange rate policies.
 - (c) A crisis preventive facility, the CMIM Precautionary Line (CMIM-PL), was introduced and was similar to various contingent credit lines at the IMF.
- (v) Decisions taken at the May 2016 meeting of the ASEAN+3 Finance Ministers and central bank governors:
- (a) Welcomed the establishment of AMRO as an international organization on 9 February 2016
 - (b) Instructed deputies to carefully study how the CMIM can be better integrated into the global financial safety net
 - (c) A task force was established to give its recommendation on increasing the IMF delinked portion by November 2016
 - (d) AMRO is to further develop the qualification indicators for the CMIM Precautionary Line based on the Economic Review and Policy Dialogue (ERPD) matrix

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