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Yves Mersch: Challenges for euro area monetary policy in early 2018

Speech by Yves Mersch, Member of the Executive Board of the ECB, at the 32nd International ZinsFORUM, Frankfurt am Main, 6 December 2017

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The Governing Council of the ECB at its October meeting decided to reduce the rate of monthly asset purchases. In my remarks today, I would like to explain the rationale behind that decision, and how it remains consistent with our mandate for price stability.

In short, as our asset holdings rise and the growth outlook improves, unchanged policy parameters actually imply greater monetary stimulus. Furthermore, I am confident that the apparent disconnect between growth and inflation is a temporary phenomenon and that inflation dynamics will increase.

It is therefore possible for us to scale back our net asset purchases, while keeping our policy sufficiently accommodative to support those inflation dynamics. If one extrapolates from the current brighter economic outlook, one cannot imagine that we would need to extend further our present purchases. A symmetric approach to our inflation mission would therefore be more appropriate than a one-dimensional promise to do more in case of deflation. Managing QExit will be challenging, however.

While ending the purchase programme quickly could provoke undue market reactions, we should not overlook the fact that the longer our asset purchase programme continues, the less effective the programme and the greater the risks attached to it become. Having a credible view of the exit is important to keep any such risks contained.

The recent policy decision

Let me begin with the adjustments to our monetary policy parameters made in the October Governing Council meeting. The asset purchase programme will be extended to September 2018, at the lower amount of €30 billion per month, or beyond if necessary, until the Governing Council sees a sustained adjustment in the path of inflation consistent with its definition of price stability.

This decision was made in an environment of robust demand growth, but with still modest increases in the underlying inflation rate. We have now benefited from 18 uninterrupted quarters of economic growth, with indicators pointing to continued robust growth. The unemployment gap – an established measure of labour market slack – is now closed, and employment has reached its highest ever level in the euro area.

In short, our monetary policy has successfully stimulated demand and returned slack resources into productive use. One would expect this strong demand to generate a marked increase in inflationary pressures. Yet this has not yet fully materialised in the euro area, although signs of inflationary pressures and limits to the lags have been constant for the last six month. Why then have we reduced our purchases before without there being a substantial adjustment in inflation?

The decision to reduce the monthly rate of purchases rests on two factors. The first involves understanding how the stimulus provided by our asset purchases evolves over time, and the second relates to the relationship between output and inflation.

The recessions caused by the global financial crisis and the sovereign debt crisis required significant monetary stimulus to counter the large degree of slack in the economy and ensure that inflation remained consistent with our price stability definition. Monetary policy also had to react to a number of headwinds, which reduced the impact of a given level of interest rates on economic demand.

Some, such as an ageing population and the slowdown in measured productivity growth, [1] are longer term in nature. Others were more temporary. The process of deleveraging pushed up desired saving, uncertainty weighed on investment and a prolonged period of low inflation threatened to de-anchor inflation expectations, with a risk of outright deflation.

But as the ongoing recovery gains momentum, the influence of these temporary headwinds is fading. Fears of deflation have dissipated. In these circumstances, unchanged monetary policy parameters would in fact imply an unwarranted increase in monetary stimulus, and when one looks at the 10-year German government bond yield since the summer one might conclude that, despite fewer purchases, we had eased our monetary policy, a step which does not correspond to our plan.

A further reason why the Governing Council elected to scale back our monthly purchases is that, as the size of our portfolio increases, the marginal impact of a given level of purchases increases. Owing to our already large bond holdings, the free float of securities is now substantially lower than when we began our programme in 2015. This increases the relative share of our purchases in the market, and therefore the impact of those purchases per billion euro spent. In other words, a slower pace of purchases today can have an equivalent effect on yields as a higher pace yesterday.

Moreover, as the stock of bonds rises, our reinvestment needs rise in tandem and we have to increase our gross purchases – that is, our net purchases plus our reinvestments; and do that in an environment of lower new borrowing in most euro area countries. This means that, even with a slower pace of net purchases, the Eurosystem will still have a substantial presence in the market. Indeed, cumulative redemptions of around €150 billion are expected in 2018.

For all these reasons, an adjustment to our policy stance was necessary at our last meeting. By the same logic, we should be able to further adjust our policy in the future as confidence increases about the robustness of the recovery without choking off growth or inflation. And the more the recovery advances, the less the economy depends on unconventional monetary policy stimulus and benefits from balance sheets repair, structural reforms and fiscal tailwinds.

As for the current rate of inflation, it is worth noting that the euro area is by no means the only developed economy exhibiting robust output growth with inflation rates below historical experience. I do not have time today to do justice to all the various explanations put forward by economists. In truth, I'm not particularly persuaded by any of them. I do not believe that such factors will prevent us from achieving our mandate over the medium term. We may take a little longer to achieve our objective, but achieve it we will.

Let me focus on just one explanation – that the relationship between domestic slack and inflation, termed the Phillips curve, has become so flat that changes in output have little effect on inflation. Prolonged periods of low inflation can reduce wage growth, since wage-setters pay some attention to past outturns. Moreover, job insecurity, digitalisation and high unemployment have encouraged unions to prioritise employment over wages. And the deep downturn has led to broader slack in the labour market – i.e. involuntary part-time and temporary work – that needs to be reabsorbed before wage pressures rise.

Yet we are going through a transition phase out of a very deep crisis, and these downward forces should wane. Indeed, the difference between the headline unemployment rate and broader measures of labour market slack has already edged down in the past two years. The share of firms that say that labour shortages are limiting their production is at its highest level ever in manufacturing and services. This is translating into higher wage growth now, and in turn contributing to a pick-up in inflation. Various measures of underlying inflation, which is key for assessing durability, appear to have turned a corner.

I say "appear", because policymakers should be humble in their pronouncements. [2] Estimates of the degree of slack in the economy vary widely and are often revised. Model outputs, however complex they may be, should be treated with due caution, and judgement based on experience remains an essential part of the policymaking process. We should avoid making unwarranted statements about points in time too far into the future over which we have little true visibility.

It also means that policy decisions not only should be based on the most likely outcome predicted by models, but should also take into account the balance of risks. There are times when the risk of inaction far outstrips the risk of action, and the prudent course is to act with vigour. Introducing asset purchases to stave off the risk of deflation is one recent example. But there are also times when the balance of risks lies in the opposite direction, and prudence dictates that policymakers should be more circumspect.

Future challenges for monetary policy

On that note, while I believe that the forces already at work should in due course bring an end to the need for asset purchases, it is a matter for the ECB's Governing Council to decide on the exact timing of such a move. Our approach should evolve in tandem with our improved expectations for developments in the real economy and ensure that our mandate for price stability is fulfilled over the medium term.

Let me instead spend a few moments considering some of the risks we face in implementing our policy over the coming years. I should also add at this point that these risks are likely to grow the longer our asset purchase programme continues.

The first risk relates to the subsiding deflationary headwinds I have already mentioned. Could it be that our current monetary setting is suddenly too accommodative? In short, because of the uncertainties and imprecisions involved in measuring slack and inflationary pressures in the economy, we might find ourselves behind the curve without realising it. Hence, through the long and variable lags of monetary policy, we will end up with inflation above the rate consistent with our price stability mandate.

This would require a sharp correction of the monetary policy settings in years to come. Yet such a correction of interest rates would pose risks to the financial sector. Banks could be hit hard as funding costs rise faster than interest income on outstanding loans.

The second risk is a related one, in that these factors could have already unwound, and inflation could turn out much higher than we expect over the course of 2018. We would find ourselves behind the curve – and realise it – but the optimal monetary policy response would involve us having to adjust our forward guidance.

This forward guidance was put in place to stabilise market expectations and to enhance the effectiveness of our asset purchases. This is because we indicate that interest rates will rise only when we are "well past" the horizon for asset purchases. So prolonging asset purchases pushes out market expectations of the first rate rise, depressing interest rate expectations across the curve. Of course, the effectiveness of that guidance also relies on market beliefs of our future actions.

In effect, forward guidance is a promise not to react to data outturns in the future so as to persuade markets to maintain low expectations for interest rates. But if we offer guidance that extends too far into the distance, beyond the point where we can form reasonable expectations about the economy, it risks unduly tying our hands unless this is backed by unanimity in the Governing Council.

This is a particular risk at present when, as I described earlier, any future increase in interest rates needs to be gradual, and hence moving late could result in policy remaining too loose for too long. Certainly as the time comes to reconsider our monetary policy stance during the course of 2018, we should reflect at length on the degree to which we wish to pre-commit ourselves.

Risks to monetary policy extend beyond the immediate outlook for inflation. Our policies have reduced the spread over risk-free interest rates paid by households and firms for their borrowing, and unblocked the flow of credit to the real economy. Such spreads are at their lowest ever level.

Yet reduced spreads may encourage investment in businesses that are only profitable at low interest rates, and such loans risk turning sour as interest rates rise. Indeed, banks and investors may be tempted to “search for yield”, without being adequately recompensed for the risk they are taking on. The normal place for monetary policy is not at the long end of the yield curve, but at the short end.

The focus of monetary policy is of course on our price stability mandate, and ensuring financial stability risks are adequately mitigated is the role of microprudential supervision and macroprudential policy. While there is little evidence at present of area-wide credit-fuelled bubbles, there are some notable localised pockets, such as in commercial real estate, and evidence of “search for yield” behaviour.

The financial crisis showed how such risks can interfere with the smooth operation of monetary policy through their effects on banks, which remain a key part of the monetary transmission mechanism in the euro area. We should therefore bear in mind that these risks could potentially complicate our ability to meet our price stability mandate in the future.

There are other longer-term risks to monetary policy, namely through the allocation of credit to both productive and unproductive firms. By reducing interest rates for all firms, monetary policy may indirectly permit inefficient firms to remain in business – becoming so-called zombie firms. This blunts the productivity-enhancing function of downturns to bring about “creative destruction”, whereby inefficient firms are forced out of business, freeing up resources to move to more efficient firms and boosting aggregate productivity. Indeed, there is evidence that creative destruction was weaker during the Great Recession than in previous downturns [3] and that zombie firms have weighed on productivity growth in some euro area countries. [4]

Productivity growth plays an important role in raising aggregate living standards, but it also affects the conduct of monetary policy. Higher productivity growth spurs investment, and expectations of higher future income encourage households to spend more today. Thus slower productivity growth requires monetary policy to lower interest rates by more than would otherwise be the case to stimulate the economy. Given that interest rates are currently low, and our stock of purchases is quite large, this would restrict our ability to respond to future downward shocks.

What I have just explained are the *economic* risks arising from a potential misallocation between productive and unproductive businesses brought about by our asset purchases. But there are also *legal* risks for the ECB regarding our Treaty obligations. Article 127 requires that we “act in accordance with the principle of an open market economy … favouring an efficient allocation of resources”. Thus, in respecting our price stability mandate, we should only do as much as is necessary, and be aware of potential side effects from running expansive policy for too long.

An important principle of an open market economy is price formation in markets through the interaction of private sector agents. It should be those interactions that ensure correct pricing, notably of credit risk, and not the interactions created by our asset purchases.

It is clear that, with the Eurosystem now owning public and private sector assets amounting to over €2 trillion, we have become a bigger player in the market than ever before. This means that we are now buying bonds from more price-insensitive investors, such as pension funds and insurance companies, bidding up the price at which we need to pay. Liquidity conditions are expected to become more challenging in certain market segments the longer the purchasing programme remains active.

As such, we have to be mindful not to exert an undue influence on price formation.

Another potential complication relates to our public sector purchases. A key safeguard that we have set up for these purchases is to operate so-called “blackout periods”, where we do not buy around the date of a new issuance. This facilitates price formation and ensures that Article 123 of the Treaty is fully respected – the monetary financing prohibition.

Mindful of self-imposed constraints in this respect the remaining space for both net and gross purchases will largely be in newly issued bonds. This poses some potential complications that we have to monitor very closely.

Conclusion

Let me conclude.

The recovery in the euro area continues at a robust pace, employment has risen strongly. Both wages and underlying inflation appear to have turned the corner.

At its October meeting, the Governing Council chose to reduce the rate of net asset purchases, which, as I have explained today, prevented an unwarranted increase in monetary stimulus. We will continue to monitor developments in the economy and set policy in a way that is consistent with our price stability mandate.

In doing so, we must also take into account the balance of risks when setting policy.

If we withdraw our monetary policy stimulus too early and too fast, asset prices could drop and yields rise sharply, with negative spill-over effects to the economy. At the same time, we have to be mindful, as our asset purchase programme continues, that the risks attached to it may increase the longer it lasts. Nourishing a market belief that the exit might be permanently postponed could exacerbate the potential cliff effects. A credible perspective on exit is needed to keep these risks contained.

A sense of proportion will therefore be crucial in managing the QExit.

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[1] See, e.g., Gordon, R. (2016), The Rise and Fall of American Growth: The U.S. Standard of Living since the Civil War, Princeton University Press. It is worth noting that others contest the slowdown, arguing it relates to measurement error, e.g. Brynjolfsson, E. and A. McAfee (2011), Race Against The Machine: How the Digital Revolution is Accelerating Innovation, Driving Productivity, and Irreversibly Transforming Employment and the Economy, Digital Frontier Press.

[2] See Mersch, Y. (2017), “Economic Policy and the Need for Humility”, speech at the Conference “Banking and Financial Regulation”, Bocconi University, 9 October.

[3] Bartelsman, E., López-Garcia, P. & G. Presidente, “Cyclical and structural variation in resource reallocation in Europe”, *mimeo*.

[4] See, e.g. See Gopinath et al. (2015): “Capital Allocation and Productivity in South Europe”, NBER Working Paper No. 21453; Borio et al. (2016): “Labour reallocation and productivity dynamics: financial causes, real consequences," Bank for International Settlements Working Papers 534; Andrews, D. & F. Petroulakis (2017), “Breaking the shackles: Zombie firms, weak banks and depressed restructuring in Europe”, OECD Economics Working Papers No.1433.

Fonte: European Central Bank (ECB)

https://www.ecb.europa.eu/press/key/date/2017/html/ecb.sp171206.en.html

Haruhiko Kuroda: Asian financial markets - 20 y since the Asian Financial Crisis, and prospects for the next 20 years

Keynote speech by Mr Haruhiko Kuroda, Governor of the Bank of Japan, at the 2017 Annual General Meeting of the Asia Securities Forum, Tokyo, 28 November 2017

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Introduction: The Past 20 Years

Good morning ladies and gentlemen. It is my great pleasure to join you this morning at the Annual General Meeting of Asia Securities Forum.

The year 2017 marks twenty years since the Asian Financial Crisis. Before the crisis, the region was highly praised for its strong economic growth. But at the same time, weaknesses had been accumulating, such as large current account deficits, high external debt, and massive non-performing loans. When a combination of economic, financial, and corporate problems triggered a sharp loss of confidence and capital outflows from the region, the crisis erupted and countries faced extreme recessions.

Twenty years later, Asia is now the largest contributor to global growth, accounting for 57 percent of global growth in real terms for 2016. [1] Domestic demand, especially consumption, has become the engine of growth and major cities in the region have prospered, being often characterized by the simple phrase, "lively and vibrant." Here in Tokyo, the surging number of Asian tourists to Japan is itself evidence for the strength of growing consumption in Asia.

I cannot but think of the significant changes that the economies of Asia, including Japan, have experienced over the past twenty years. These changes have been made possible through countless painstaking efforts, initiatives, and policies that countries in the region have introduced, both individually and collectively. I myself have been at the forefront of policy making in orchestrating crisis responses and enhancing regional cooperation in Asia for almost two decades, at Japan's Ministry of Finance, the Asian Development Bank (ADB), and the Bank of Japan (BOJ). Confirmation of the region's greater resilience against a major economic shock is deeply reassuring.

Let me touch upon the responses taken in the region after the crisis two decades ago. First, Asian countries improved their current account balances and strengthened foreign exchange reserves. The increase in net external assets has enhanced resilience against possible capital outflows. Second, the ratio of non-performing loans has decreased, and regulatory and supervisory frameworks have been strengthened. Third, many countries in the region have adopted more flexible exchange systems. Last but not least, financial markets, especially local currency bond markets, have continued to develop.

The development of local currency bond markets was aimed at addressing two issues. One was the so-called double mismatches, that is, currency mismatches and maturity mismatches, and the other was a bank-centric financial system. Financial institutions in the region were borrowing short-term debt in dollars to finance longer-term lending in domestic currencies. This double mismatch was particularly damaging as the significant depreciation of their currencies inflated borrowers' debt burden. This led foreign lenders to refuse rolling short-term debt, which then triggered massive defaults of banks and firms. Twenty years later, the degree of the double mismatches has been reduced. Local currency bond markets have grown, as can be seen in Chart 1, providing an alternative intermediation channel to bank-financing. Today, the capitalization of Asian local bond markets is equivalent to 3.7 trillion U.S. dollars, more than 100 times larger than before the crisis. [2] We have certainly made progress. Economies have become more resilient to exogenous shocks, and the financial sector has developed significantly.

In addition to these individual efforts, various initiatives have been established through regional cooperation. For example, a regional financial safety net, the Chiang-Mai Initiative Multilateralization, has been set up by the ASEAN countries, together with China, Japan, and Korea, or ASEAN+3. The Asian Bond Market Initiative (ABMI) was launched in 2002 by ASEAN+3, and this has contributed to the development of local currency bond markets. Market associations and self-regulatory organizations, such as yourselves, have also played an important part in enhancing the efficiency and transparency of the markets.

Challenges Remaining

However, important challenges still remain. Today, I will focus on the importance of further developing local currency bond markets, partly because I am surrounded here by people from the securities industry.

As I have mentioned, local currency bond markets have grown over the last twenty years. At the same time, bank financing still dominates as a primary source of funding in the region. You can see this from Chart 2. Bank credit, as a source of corporate funding, has outgrown both stock market capitalization and corporate bonds outstanding over the years.

The strong reliance on bank-financing may be explained by Asian corporate culture, which puts high priority on business relationships. Bond financing is often not the first choice for domestic firms when financing their business. To make my point clear, I am not proposing that Asian corporates should rely on market-financing over bank-financing, as is the case in some other countries. I would rather like to stress the importance of diversifying the sources of funding to reduce the direct effect on the corporate sector, should the banking sector face economic or financial shocks.

Along with this cultural issue, domestic firms are deterred by the cost of bond-financing when compared with bank loans. One of the factors that explain the unattractiveness of bond-financing may be the lower levels of market activity and less liquidity in the secondary market. With lower liquidity in the secondary market, investors require additional premiums, which increase the cost of issuance. In such an environment, domestic firms are more likely to rely on banks for financing.

In this regard, developing highly efficient and liquid local currency bond markets is essential. Past initiatives in the region have enriched the primary markets. We may therefore need to put more focus on developing liquid secondary markets.

As presented in Chart 3, according to a survey conducted by Asian Bonds Online, there is no single factor that inhibits the development of the secondary markets. Survey respondents were asked how important each of the eight structural issues was, with respect to local currency bond market liquidity. The survey results in recent three years show that "Greater Diversity of Investor Profile" was the most important structural issue for promoting the market liquidity. Another structural issue, "Transaction Funding," which also marked a relatively high score, may also be worth noting as an important impediment.

Let me elaborate these two structural issues. First, the issue of investor base diversification. Since banks are the dominant financial institutions in the region, they are often the largest investor group as well. The presence of buy-and-trade investors like mutual funds, and active investors like hedge funds is relatively low, and this may be one of the causes of low liquidity in the secondary market. But it has to be borne in mind that merely increasing the size of the domestic investor base does not necessarily improve market functioning. In the region, demand for local currency bonds exceeds supply. In this situation, if a few dominant buy-and-hold type investors become even larger, they may take bonds out of circulation, leaving fewer investable bonds in the market. It is therefore important to increase the variety of investor types, attracting those who have different investment objectives and strategies.

The second issue is that of transaction financing. Improving it would require the development of repo markets. Repo markets are a key instrument for banks to trade cash while controlling counterparty risks. A well-functioning repo market is also a precondition for feasible market-making by dealers, and would increase two-way trading in both equity and bond markets. However, repo transactions in many Asian emerging markets are still restricted or small in transaction volume, as uncollateralized short-term funding conditions are easy and many investors do not have the incentive to use such instruments.

I have discussed the importance of developing local currency bond markets from the viewpoint of preparing for exogenous shocks and adverse circumstances. I would like to add another perspective related to the main theme of this meeting, "Ways for building a sustainable future."

It has often been said that, in order to achieve sustainable growth, the region must narrow its large infrastructure gaps. The ADB estimates that this will require funding of over 1.7 trillion U.S. dollars a year, through 2030. [3] This magnitude of financing is well beyond the current funding capabilities of individual national governments, international organizations, and banks that operate as project finance lenders in the region.

In the financing of infrastructure assets, bond finance offers a number of advantages over bank loan finance. Infrastructure assets often generate stable long-term cash flows that make infrastructure debt an attractive investment opportunity for bond investors. Insurers and pension funds who have long-dated liabilities are seeking to match them with long-dated assets. Bond markets are able to provide opportunities to issue longer-tenor debt at fixed interest rates, thereby reducing the risks associated with refinancing shorter-tenor debt and the necessity of having to enter into long-term interest rate swaps to manage the risk of interest rate fluctuation. Also, as revenues from most infrastructure projects are denominated in local currencies, local currency infrastructure bonds will be able to mitigate the risk of currency mismatch.

Central Banks' Initiatives

Let me now explain some measures taken by central banks in the region. Along with the Ministries of Finance, central banks of ASEAN+3 are taking part in the ABMI that I mentioned earlier, and have contributed especially to the discussion of cross-border payment and settlement issues.

Furthermore, the Executives' Meeting of East Asia Pacific (EMEAP) central banks, a group of 11 central banks and monetary authorities in the East Asia and Pacific region, set up the Asian Bond Fund (ABF) initiative in 2003, in order to develop local currency bond markets. The region has seen several advancements since the launch of the ABF initiative. They include (1) accelerated tax reforms to exempt nonresident investors from withholding tax, (2) enhancement of the regulatory framework for exchange-traded funds, (3) liberalization of foreign exchange administration rules, (4) improvements in regional market infrastructure, and (5) the adoption of documentation in line with international best practices. These advancements could perhaps have been achieved sooner or later without the ABF initiative, but the initiative certainly had a positive effect in facilitating these developments. [4]

The EMEAP central banks have also been engaged in promoting analysis of financial market developments in the region. In 2014, EMEAP published a report that assessed the developments and challenges in the repo markets in the region. [5] In addition to the benefits of efficient repo markets that have been noted, repos are an essential instrument in the open market operations of central banks, and therefore important to the transmission of monetary policy. The deeper these markets are, the more scope they offer central banks in their liquidity management operations.

Along with intra-regional initiatives, individual central banks have also introduced measures aimed at facilitating repo transactions. For example, the Monetary Authority of Singapore launched the Securities Repo Facility to promote their market-making activities. The central banks in Malaysia, Thailand, and Indonesia, have set up programs to increase awareness of repo markets among market participants, including corporate treasuries. Many other central banks are also working with investors, issuers, and intermediaries, to assess what can be done to facilitate active repo markets.

We, at the BOJ, have been participating in discussions at EMEAP to enhance the ABF initiative, and have been active in conducting market reviews. Assistant Governor Maeda of the BOJ currently chairs the Working Group on Financial Markets, leading further work in this area. The Bank also contributes to capacity-building with other authorities.

Concluding Remarks: Initiatives for the Next 20 Years

I have discussed the importance of developing local currency bond markets, its remaining challenges, and initiatives taken by central banks in the region. Let me now summarize some of the wide range of benefits that can be gained by developing deep and liquid local currency bond markets. First, it makes possible for governments and firms to borrow in local currencies at longer maturities. This will reduce the risks associated with currency and maturity mismatches. Second, the development of such bond markets will enable borrowers to diversify their sources of funding by complementing bank-financing. At the same time, investors will gain more investment opportunities. With enhanced investment opportunities, abundant savings in the region could be recycled within the region. It could also fill part of the large infrastructure funding gap. Lastly, well-functioning primary and secondary bond markets reinforced by an expanded investor base will improve the overall efficiency of financial markets, which in turn will aid macro-economic policy implementation.

Over the past two decades, there have been many fruitful initiatives and programs to develop local currency bond markets. However, this is still work in progress and more needs to be done. As the market is a place of interaction, all stakeholders must play their roles. A successful implementation strategy must identify critical paths and appropriate sequencing to achieve the optimal result. Cooperation among authorities and private market participants is the key to further development.

The ASEAN+3 Bond Market Forum (ABMF) was set up in September 2010 by the ASEAN+3 countries as a common platform to foster standardization of market practices and harmonization of regulations related to cross-border bond transactions in the region. Members comprise experts drawn from both public and private sector organizations, such as those present at this forum today. This type of forum is a practical step toward achieving the ultimate common goal of Asia's bond market development.

The global economy continues to recover and the financial system has been maintaining stability. As the IMF's Managing Director expressed in her Global Policy Agenda at the last International Monetary and Financial Committee (IMFC) meeting, current economic and financial conditions provide "a window of opportunity" to tackle key challenges. Stakeholders in the region must maintain the will to further develop and deepen the market. Through these concerted efforts, the challenges in fostering bond markets can be overcome.

On the 10th anniversary of the Asian Financial Crisis, at a BOJ symposium, the then Governor Zeti of Bank Negara Malaysia, stated: Asia, especially the ASEAN tigers, is back and poised to leap on to the next wave of economic advancement and prosperity. [6] How correct she was. Asia's economy has developed much more vigorously than many had anticipated. Economic integration in the region has further deepened through the development of global value chains.

Looking ahead to the next twenty years, Asia's economy will continue to be at the core of world economic growth and we will experience further integration. Along with such developments, it is natural to seek more developed and integrated regional financial markets. We can anticipate that twenty years from now, Asia's financial markets will have developed to become as efficient and liquid as other major financial centers in the world.

Thank you for your kind attention.

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[1] The percentage share is based on real GDP (constant 2010 U.S. dollars), taken from the World Bank's World Development Indicators. "Asia" in this context includes Asia & Pacific and South Asia.

[2] The total is as of June 2017 and covers nine countries and regions, including China, Hong Kong, Indonesia, Korea, Malaysia, the Philippines, Singapore, Thailand, and Vietnam. The scaling factor compares June 2017 with June 1997 with reference to comparable four countries and regions, including China, Hong Kong, Korea, and Thailand. Data are taken from Asian Bonds Online.

[3] ADB (2017), Meeting Asia's Infrastructure Needs.

[4] For example, see Mizen, P., and Tsoukas, S. (2014), "What Promotes Greater Use of the Corporate Bond Market? A Study of the Issuance Behaviour of Firms in Asia," Oxford Economic Papers, Vol. 66 (1), pp. 227-253.

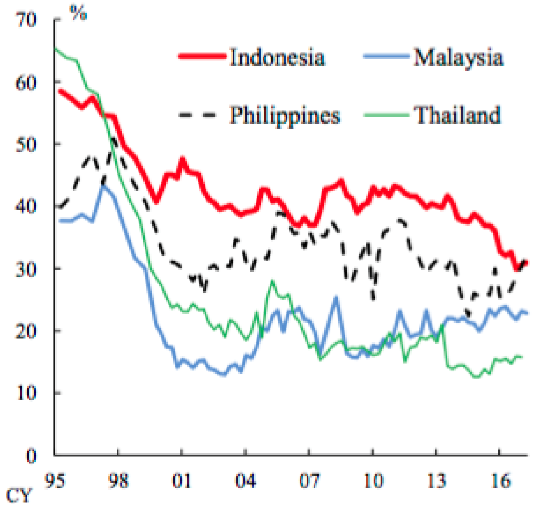
[5] EMEAP Repo Markets: State of Play -- A Report by the EMEAP Working Group on Financial Markets 2014 (available from http://www.emeap.org/index.php/publications/).

[6] "Ten Years after the Asian Currency Crisis: Future Challenges for Asian Economies and Financial Markets," a speech at the international symposium hosted by the Center for Monetary Cooperation in Asia (CeMCoA) of the BOJ on January 22, 2007 in Tokyo (available from https://www.boj.or.jp/en/announcements/release_2007/index.htm/).

Chart 1

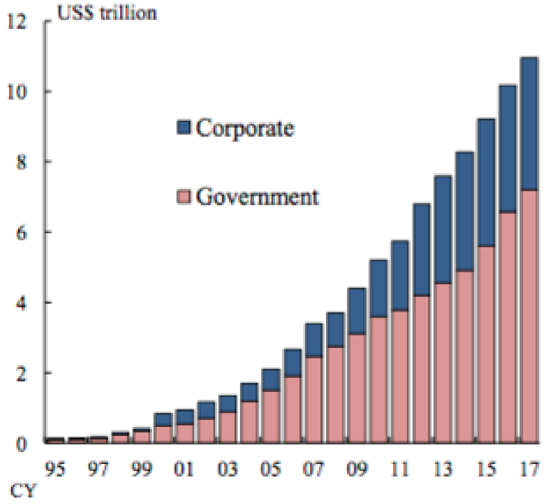
Increased Resilience

Less reliance on foreign-currency-denominated short-term funding



Notes : 1. The figures are the ratios of foreign currency-denominated short-term claims to all claims of foreign banks.
2. The latest data are as of end-June 2017.
Source: BIS.

Growth of Asian local currency bond markets

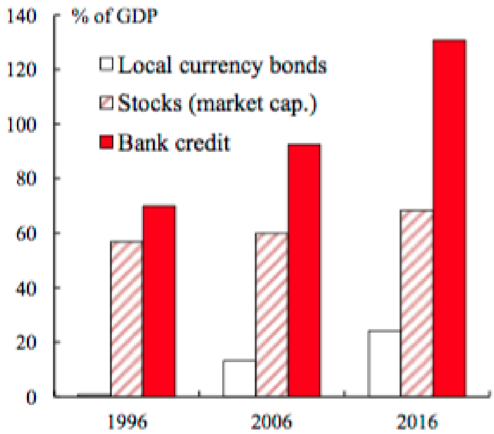


Notes: 1. Aggregates of China, Hong Kong, Indonesia, Korea, Malaysia, Philippines, Singapore, Thailand, and Vietnam.
2. The figures for 2017 are as of end-June 2017.
Source: *Asian Bonds Online*.

Chart 2

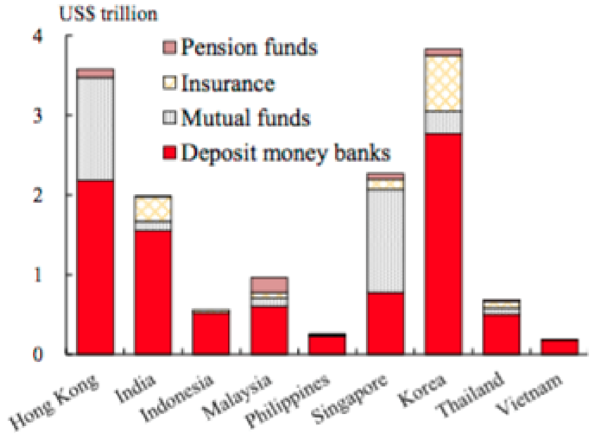
Bank-Dominated Financial Systems

Corporate financing in Emerging Asia

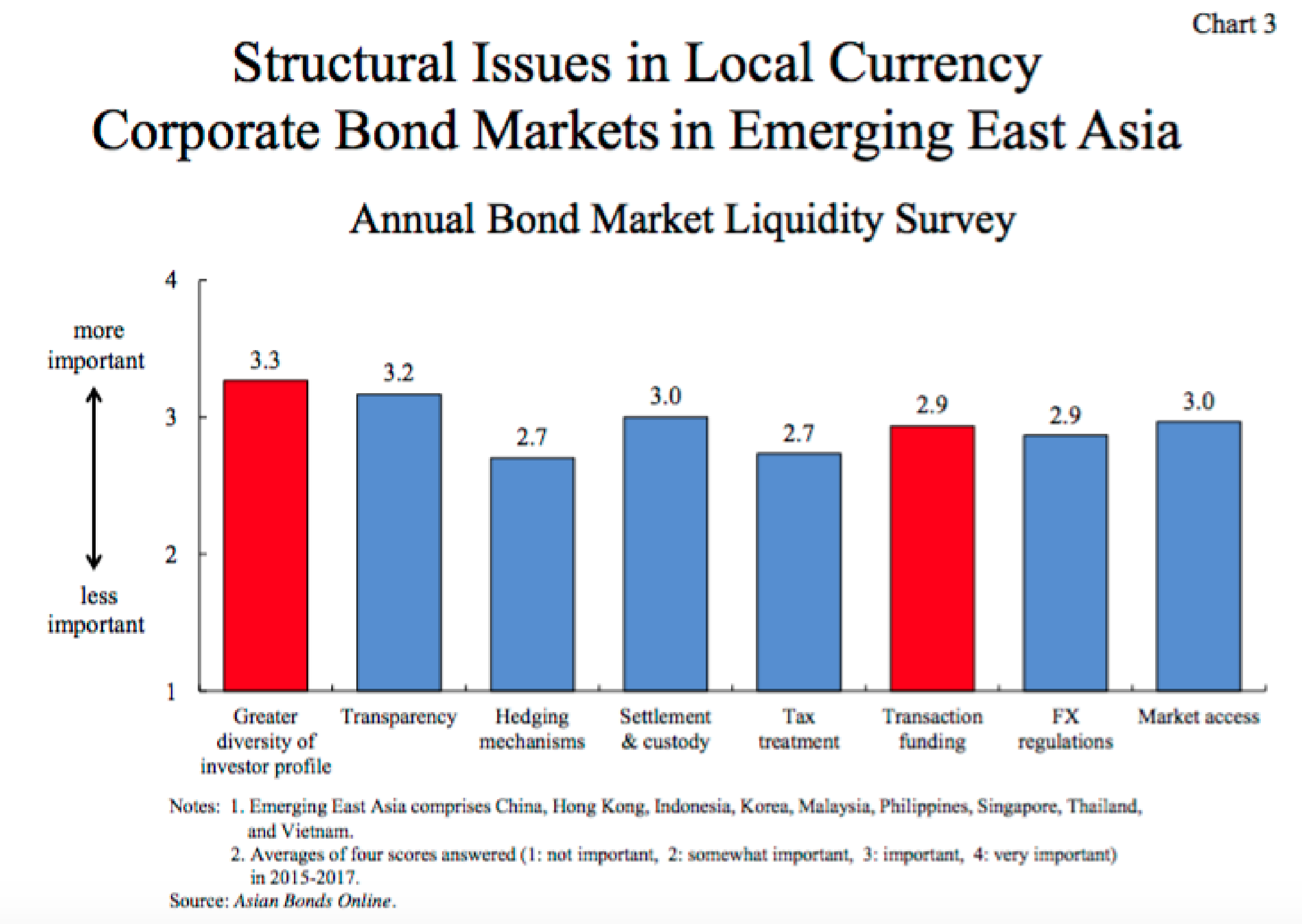


Note: Emerging Asia is the aggregate of China, India, Indonesia, Korea, Malaysia, Philippines, Thailand, and Vietnam.
Sources: *Asian Bonds Online*; The World Bank, *World Development Indicators*.

Investor base in Emerging Asia



Notes: 1. As of end-2013 except for India's deposit-money-banks figure which refers to end-March 2014.
2. Figures for Pension funds and Mutual funds for Indonesia and Vietnam and Insurance for Hong Kong are not available.
Sources: The IMF, *International Financial Statistics*; National central banks; The World Bank, *Global Financial Development Database*.



Fonte: Bank For International Settlements (BIS)

https://www.bis.org/review/r171205d.pdf