



THE ADVISORY GROUP ON APEC FINANCIAL SYSTEM CAPACITY-BUILDING

First Meeting 2012

23 February 2012

Hong Kong, People's Republic of China

Meeting Paper 3-B Asian Financial Markets Integration (State Street)

Purpose: For information

Issue: Financial Markets Integration

Background:

The region is made up of a range of diverse markets at different levels of development but rapid growth is a common feature. To take full advantage of the potential in the Asia Pacific a solid financial foundation needs to be built. Greater coordination would make markets more efficient, increase the products/services offered and encourage cross border flows. Business would be able to expand their presence and offerings in individual markets. Consumers would be able to access a broader range of products and services at lower cost. Governments could better recycle savings within the region and build domestic financial markets.

Finance Ministers do not have control over some of the key issues that will determine whether integration succeeds, including tax, customs, legal reform and currency controls. ASEAN takes an opt-in approach where member countries can choose to join an initiative or sit out. A lack of coordination between ASEAN and other regional organizations risks greater complexity and fragmentation across the broader region.

Proposal/Recommendation:

Catalogue work of existing organizations; Determine where this initiative fits in;
Get business and regulators to identify common priorities; Look for ways to complement rather than compete with existing initiatives; Leave G20, Basel, IOSCO to deal with enhanced regulation; Focus on developing individual markets and cross border trade.

Decision Points: Note the presentation.

Asian Financial Markets Integration

The Advisory Group on APEC Financial System Capacity Building

23 February 2012

Hong Kong

Hon Cheung
Regional Director
Official Institutions Group, Asia



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Investment Management | Investment Research and Trading | Investment Servicing

Agenda

Arguments in Support of Integration

Issues to Consider

Key Challenges

Fund Sector Example

Listed Product Example

ASEAN Example

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Arguments in Support of Integration

- The region is made up of a range of diverse markets at different levels of development but rapid growth is a common feature
- To take full advantage of the potential in the Asia Pacific a solid financial foundation needs to be built
- Greater coordination would make markets more efficient, increase the products/services offered and encourage cross border flows
- Business would be able to expand their presence and offerings in individual markets
- Consumers would be able to access a broader range of products and services at lower cost
- Governments could better recycle savings within the region and build domestic financial markets

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Issues to Consider

- How APEC initiative will link into other organizations
 - e.g. EMEAP, IOSCO, ADB, ASEAN
- How this project will fit with other initiatives in the region
 - e.g. ABMI, ARFP, ASEAN Exchanges
- Sectors of focus
 - e.g. Banking, Securities, Insurance
- Priority products
 - e.g. Bonds, Exchange Traded Products, Collective Funds
- Focus
 - e.g. Financial Regulation or Liberalization, efficiencies in market practices, cross border products and services

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Key Challenges

- Perceived threat to national interest in individual jurisdictions
- Overcoming differences in regulations in each jurisdiction
- Lack of free currency convertibility and a unified currency
- Agreeing to treatment of foreign investors and amending tax regulations
- Different levels of development and capacity in markets across the region
- Overlap with other initiatives and organizations in the region

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Fund Sector Example: Funds Passporting Idea

- No cross-border fund vehicle in the region and limited cross-border recognition of products

- Easier to offer EU-regulated UCITS products in the region than a product from one regional jurisdiction to another

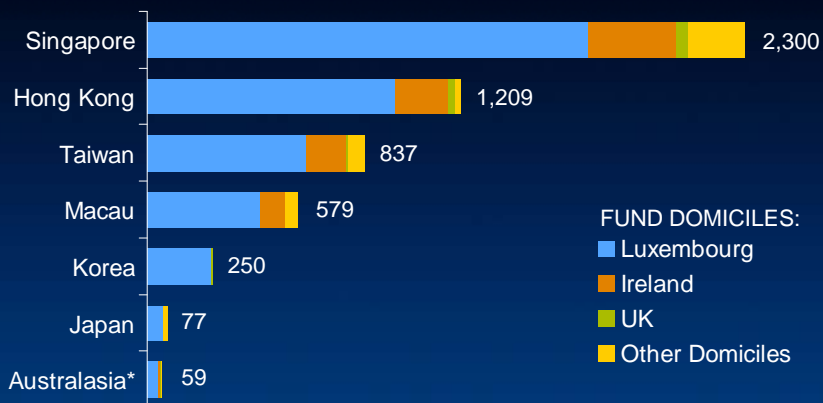
- Penetration of UCITS products in some regional markets suggests fund passporting can work if regulators are comfortable

- Lack of penetration of UCITS products in other markets suggests an alternative to UCITS is needed to unlock regional funds

- A Regional Funds Passport might give regulators the comfort they need to increase cross-border recognition of regional products

Fund Sector Example: External Products Dominate

**Cross-Border Fund Registrations in Asia Pacific:
Distribution Markets and Fund Domiciles**



*Includes Australia, New Zealand and Cook Islands

Source: PricewaterhouseCoopers, *Global Fund Distribution 2010*

Fund Sector Example: Limited Cross Border Funds

Asia Ex-Japan Collective Funds Assets Under Management by Domicile

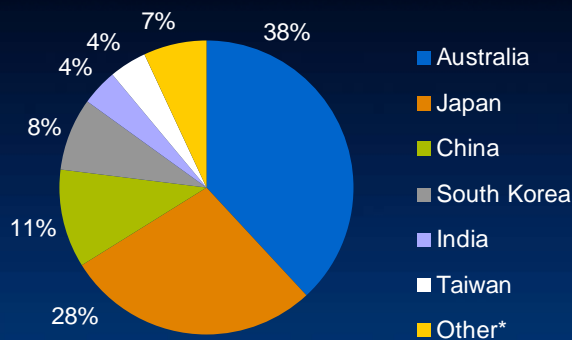


Source: Cerulli Associates, Asian Distribution Dynamics 2010, September 2010 (Numbers rounded)

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Fund Sector Example: Markets Share Assets

Asia-Pacific Collective Funds Market: Estimated Total Assets of \$3.9 Trillion



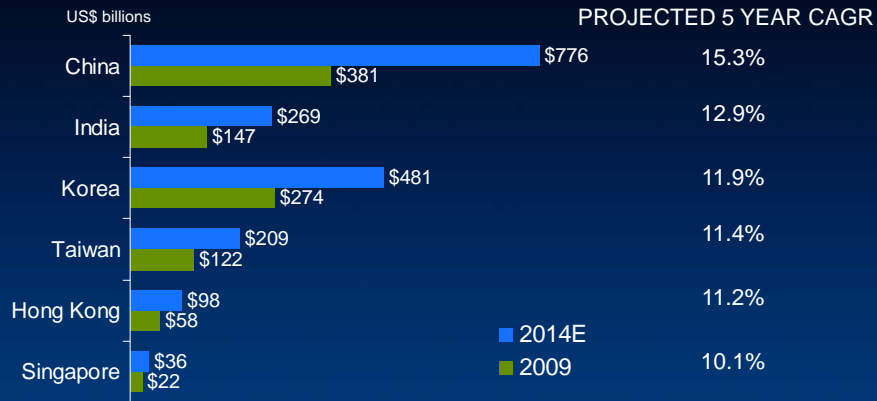
*Includes Malaysia, Hong Kong, Thailand, Singapore, New Zealand, Indonesia and Philippines

*As of December 31, 2009. Sources: Cerulli Associates, Investment Company Institute, Industry Associations and State Street estimates

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Fund Sector Example: Assets Expected To Grow

Projected Collective Fund Assets Under Management for Select Emerging Markets 2009-2014



Source: Cerulli Associates, *Asian Distribution Dynamics*, September 2010

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Fund Sector Example: 4 Options Being Examined

- APEC Asian Regional Funds Passport Initiative (ARFP)
- ASEAN Collective Investment Scheme Initiative (CIS)
- Greater Acceptance of UCITS and Traditional Cross Border Products
- Expansion of Domestic Funds Sector

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Fund Sector Example: Essence of Proposals

- Product Manufacture in Regional Countries
- Domicile and Custody in Regional Countries
- Management of Products In Regional Countries
- Sale of Products to Regional Countries

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Fund Sector Example: APEC Initiative

- Initiated by Australia following the "Australia as a Financial Centre Report"
- Investigation supported in Nov 2010 APEC Finance Ministers' statement
- Various discussions in 2011 in APEC Business Advisory Pathfinder Project
- Meetings of APEC regulators in Hong Kong, Singapore, Malaysia in 2011
- Support for further work at Nov 2011 APEC Finance Ministers' Meeting

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Fund Sector Example: ASEAN Initiative

- Part of the ASEAN Economic Community (AEC) Plan of 2015

- Being pursued under the Capital Markets Implementation Plan

- Discussions under way amongst ASEAN regulators

- Early agreement by a few countries by 2012 proposed

- Possible announcement at April 2012 ASEAN Finance Ministers' Meeting

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Listed Products Example: Lessons from PAIF

- What is PAIF?**
- The ABF Pan Asia Bond Index Fund (PAIF)
 - Exchange-traded bond fund investing primarily in local currency government and quasi-government bonds in eight Asian markets
 - Domiciled in Singapore and listed in Hong Kong and Japan
 - Perhaps the only regionally domiciled large fund offering that can be offered across a wide range of Asian jurisdictions
-
- Key Learnings**
- Cross-border recognition across several jurisdictions has been successfully done before and can be done again
 - Regulators must cooperate to overcome regulatory and administrative barriers
 - Cooperation is possible when governments are motivated to act together
 - Can begin with only a few jurisdictions

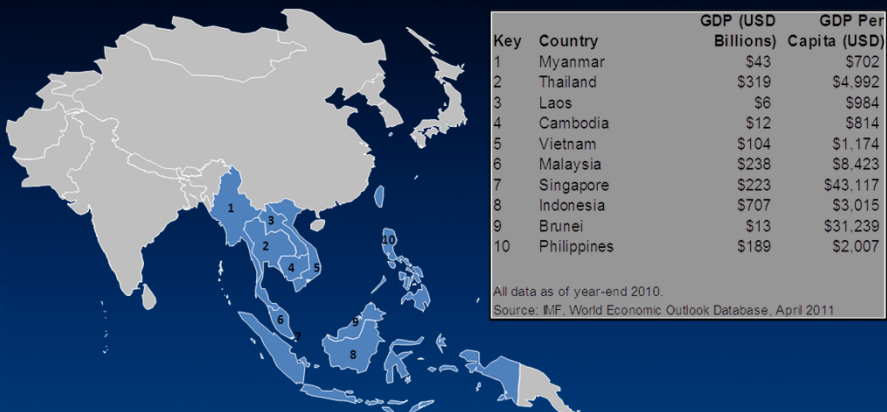
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ASEAN Example: Capital Markets Integration Plans

- ASEAN is seeking to achieve capital market integration by 2015
 - Part of the broader ASEAN Economic Community (AEC) plan
- Intend to create a network of mutual recognition agreements and harmonized regulations rather than a EU structure of political and economic unity
- The Capital Markets Implementation plan has three main themes:
 - Regional integration through harmonization
 - Development of market infrastructure and regionally focused products and intermediaries
 - Strengthening of the implementation process through a greater role for the ASEAN Secretariat

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ASEAN Example: A Diverse Region



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Figure 3: ASEAN Example: Initiatives

Initiative	Brief Overview
<i>Equity Exchanges</i>	<ul style="list-style-type: none"> A collaboration of seven stock exchanges (from the six countries of Indonesia, Malaysia, the Philippines, Singapore, Thailand and Vietnam) to create an integrated, ASEAN-branded market where ASEAN products are viewed as an asset class that investors can trade freely on any ASEAN exchange. The ASEAN Stars Initiative is a first step and lists 30 stocks from each exchange, ranked in terms of market capitalization and liquidity.
<i>Monitoring Financial Integration</i>	<ul style="list-style-type: none"> Establishes a Macroeconomic and Finance Surveillance Office (MFSO) at the ASEAN Secretariat that will be responsible for implementing macroeconomic surveillance in ASEAN and monitoring regional economic integration.
<i>Chiang Mai Currency Swap Initiative</i>	<ul style="list-style-type: none"> Establishes the ASEAN +3 Macroeconomic Research Office (AMRO), an independent regional monitoring and surveillance unit in Singapore, as part of the Chiang Mai Initiative Multilateralisation (CMIM). The newly created AMRO will monitor developments in the region such as the need for swap lines to be activated.
<i>The ASEAN Bond Markets Initiative (ABMI)</i>	<ul style="list-style-type: none"> In progress for some time, the ABMI creates local-currency denominated bond markets in the region. Efforts are also under way with the Asian Development Bank, under the sponsorship of the Japanese government, to catalogue and improve post-trade and settlement practices.
<i>ASEAN and Plus Standards Scheme</i>	<ul style="list-style-type: none"> Facilitates cross-border offerings of plain equity and debt securities within ASEAN and is available to ASEAN and non-ASEAN issuers making offerings within ASEAN. Standards based on international securities, accounting and auditing standards; and additional standards required by some ASEAN jurisdictions due to individual market practices, laws or regulations.
<i>Collective Investment Schemes (CIS)</i>	<ul style="list-style-type: none"> Discussions are under way to permit the sale of Collective Investment Schemes (CIS) across ASEAN by 2015. It is unclear if the initiative will only apply to schemes created, domiciled and managed within the region or if it will extend to products outside of the region such as European UCITS. Initiative appears to overlap with the creation of an Asian regional funds passport, and effort being pursued within the broader Asia Pacific Economic Cooperation (APEC) group.
<i>Market Professionals</i>	<ul style="list-style-type: none"> Promotes the harmonization of accounting and auditing standards and mutual recognition of certification and qualification of market professionals. If an agreement could be reached about allowing sales and marketing activities across ASEAN countries, the distribution of products and services would become much easier, to the benefit of consumers and companies.

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ASEAN Example: The Challenges To Integration

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Recommendations

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