

LEGISLATIVE COUNCIL PANEL ON FINANCIAL AFFAIRS
BRIEF

HONG KONG'S PARTICIPATION IN
CHIANG MAI INITIATIVE MULTILATERALISATION

PURPOSE

This paper briefs Members on Hong Kong's participation in the multilateralisation of the Chiang Mai Initiative (CMI) under ASEAN+3¹.

BACKGROUND

2 The CMI is a regional emergency liquidity facility introduced in May 2000 to provide short-term balance-of-payments support to regional economies facing liquidity shortages through a network of bilateral swap arrangements among the ASEAN+3 members. In May 2007, the ASEAN+3 Finance Ministers agreed to multilateralise the CMI which would be governed by a single contractual agreement to increase its effectiveness. The objective of CMI Multilateralisation (CMIM) is to

¹ ASEAN+3 comprises the 10 ASEAN member states (Brunei, Cambodia, Indonesia, Lao PDR, Malaysia, Myanmar, the Philippines, Singapore, Thailand and Vietnam) together with China, Japan

provide a more advanced framework of regional liquidity support mechanism which would supplement existing international financial arrangements.

3 As the global financial crisis intensified towards the end of 2008, the ASEAN+3 Finance Ministers agreed in February 2009 to increase the size of the CMIM from the initially agreed level of US\$80 billion to US\$120 billion. The Finance Ministers further reached agreement on the main CMIM components at their meeting on 3 May 2009. These included the contribution and borrowing amount and the broad decision-making mechanism. The Finance Ministers also announced in a Annex Joint Media Statement (Annex) that they welcomed Hong Kong to participate in the CMIM.

HONG KONG'S PARTICIPATION IN CMIM

4 It is of strategic importance for Hong Kong to participate in the CMIM:

- (a) The CMIM is the newest, most important regional joint-defence mechanism to provide financial resources to participating party(ies) in the event of short-term liquidity difficulties. Out of the 14 CMIM participants, five of them (China, Japan, Korea, Singapore and Hong Kong, China) rank among the world's top ten largest

and Korea.

holders of foreign currency reserves and together account for roughly 50% of global reserves. Being a major international financial centre and one of the largest reserves holders in the region, it is desirable for Hong Kong to show solidarity and join this joint-defence mechanism.

(b) The participation has substantial practical and symbolic importance to Hong Kong's financial stability. The CMIM aims to provide temporary liquidity to participants in need, and in doing so helps mitigate the risk of financial contagion. The experience of the Asian financial crisis had shown how quickly external shocks can be transmitted between economies within the region with considerable speed and impact. Guarding against such contagion is especially important for an open economy like Hong Kong which is susceptible to massive cross-border fund flows triggered by events in our neighbouring economies in the region. The establishment of the CMIM is also a powerful demonstration to international markets of the willingness of the regional economies to work together to overcome short-term liquidity issues so as to promote overall financial stability in the region. Furthermore, if Hong Kong stays out of the CMIM, it would become a clear outlier and more exposed to speculative attacks in future.

(c) Hong Kong's separate participation in the CMIM is another practical demonstration of Hong Kong's autonomy in international financial affairs under the concept of the "One Country, Two

Systems”. Hong Kong has in fact participated in some regional and international liquidity support arrangements before. These include the US Treasury Repo Agreements with central banks in Asia-Pacific region, the US\$1 billion Thailand financing package during Asian financial crisis², New Arrangements to Borrow of the International Monetary Fund (IMF)³, Currency Swap Agreement with the People’s Bank of China and a Bilateral Liquidity Arrangement with De Nederlandsche Bank.

MODALITY OF HONG KONG’S PARTICIPATION

5 The modality of Hong Kong’s participation in CMIM, as agreed by the ASEAN+3 Finance Ministers in May 2009 and approved by the Financial Secretary in October 2009, is as follows:

- (a) Financial contribution – **Hong Kong undertakes to commit, on a callable basis, up to US\$4.2 billion** (i.e. 3.5% of the total of US\$120 billion). The level of commitment is largely in line with

² In September 1997, Hong Kong participated in a financing package organised for Thailand by the International Monetary Fund. The financing package was in the form of a currency swap agreement of US\$1 billion between the Bank of Thailand and the Hong Kong Monetary Authority (HKMA). The loan earned interest at the prevailing market rate and was fully repaid in July 2003 which was a year ahead of schedule.

³ Established in November 1998, the New Arrangements to Borrow (NAB) is a set of credit arrangements between the IMF and 26 member countries and institutions to provide supplementary resources of up to SDR 34 billion (about US\$54 billion) to the IMF to forestall or cope with an impairment of the international financial system or to deal with an exceptional situation that poses a threat to the stability of that system. Hong Kong participates in the NAB with a credit arrangement of SDR 340 million (about US\$543 million or 1% of the total size of the facility).

those of Hong Kong's regional peers of similar economic size, namely the "ASEAN-5"⁴.

- (b) Form of lending – The lending will be structured as a currency swap under which the Lender will **provide US dollars in exchange for the domestic currency of the Borrower**. Interest will be charged at the prevailing market rate.

- (c) Maximum borrowing amount – Currently, 20% of each participant's borrowing quota need not be tied to an IMF facility (i.e. "IMF de-linked portion"). Hong Kong may borrow the "IMF de-linked portion" of its borrowing quota⁵ directly from CMIM up to **US\$2.1 billion**. The "IMF de-linked portion" may be increased to above 20% when the CMIM surveillance mechanism becomes fully effective in its function.

- (d) Decision-making – **Hong Kong can vote on lending decisions**, which involve issues directly related to the financial contribution of the participating economies in the CMIM (such as lending, renewal and default decisions). Lending decisions will be made by the CMIM participants by majority voting.

⁴ "ASEAN-5" comprises Indonesia, Malaysia, the Philippines, Singapore and Thailand. Apart from the Philippines which will undertake to commit US\$3.68 billion, the other ASEAN-5 economies will each commit US\$4.77 billion to the CMIM.

⁵ Hong Kong's borrowing is limited to the "IMF de-linked portion" because it is not a member of the IMF. Pursuant to the IMF's Articles of Agreement, the IMF membership is limited to sovereign states.

WAY FORWARD

6 The ASEAN+3 members are now finalising the operational details and formal documents of the CMIM with a view to launch this arrangement in the next few months.

Hong Kong Monetary Authority

October 2009

**The Joint Media Statement of
The 12th ASEAN+3 Finance Ministers' Meeting
3 May 2009, Bali, Indonesia**

Introduction

1. We, the Finance Ministers of ASEAN, China, Japan and Korea (ASEAN+3), convened our twelfth meeting in Bali, Indonesia, under the co-chairmanship of H.E. Korn Chatikavanij, Minister of Finance of Thailand and H.E. Jeung-hyun Yoon, Minister of Strategy and Finance of the Republic of Korea. The President of the Asian Development Bank and the Secretary General of ASEAN were also present at our meeting.
2. We exchanged views on regional economic and financial development and policies. We also reviewed the progress of regional financial cooperation initiatives, including the Chiang Mai Initiative Multilateralisation (CMIM), the Asian Bond Markets Initiative (ABMI) and the ASEAN+3 Research Group. Furthermore, we explored ways to further enhance these initiatives for higher efficiency and more positive impact
3. In particular, we are pleased to announce that we have reached agreement on all the main components of the CMIM, and decided to implement the scheme before the end of the year.

Recent Economic and Financial Development in the Region

4. We noted that the Asian economies, which have registered solid growth since the 1997 financial crisis, have faced significant challenges arising from the sharp contraction of the global economy. The deepening global economic downturn, coupled with heightened risk aversion in financial markets, adversely impacted trade and investment in the region. We also noted challenges posed by the downside risk factors, including further financial stress and emerging protectionism. Therefore, the current global situation requires more concerted efforts to enhance confidence, maintain financial stability, and prevent further decline in economic growth. In addition, the spread of the new health threat of influenza A (H1N1) requires us to stay vigilant on the possible impact.
5. We welcomed the outcomes of the London Summit on 2nd April 2009, which intends to restore growth and jobs, to strengthen financial supervision and regulation, to strengthen our global financial institutions, to resist protectionism and promote global trade and investment, and ensure a sound and sustainable recovery for all. We stressed the importance of the roles played by Multilateral Development Banks (MDB) in restoring growth through supporting the

areas of infrastructure and trade balance and addressing development agenda. We reiterated our call for prompt implementation of the Fifth General Capital Increase of the Asian Development Bank (ADB) and expected the augmented ADB capital base be appropriately utilized to fulfill its role in Asia, especially during this global economic slowdown.

6. We also welcomed the proactive policy measures including economic stimulus undertaken by each member country in the concerted efforts to sustain financial stability and restore economic growth and development. In addition, we recognized the importance of conducting economic policies cooperatively and responsibly to ensure sustainable economic recovery of our region given the current volatile global economic situation. We agreed to strengthen the financial system of each country and promote the flow of capital in our region. Furthermore, we agreed to further strengthen our regional financial cooperation in order to ensure financial stability and foster market confidence in our region.

Strengthen Regional Financial Cooperation

7. On **the Chiang Mai Initiative (CMI)**, we have reached agreement on all the main components of the CMIM, including the individual country's contribution, borrowing accessibility, and the surveillance mechanism. The agreed components of the CMIM, which is a framework of mutual assistance among ASEAN+3 countries, are consistent with its two core objectives : (i) to address short-term liquidity difficulties in the region and (ii) to supplement the existing international financial arrangements.
8. We agreed to implement the CMIM before the end of this year. In this regard, we tasked our Deputies to work out the operation details and implementation plan, particularly the legal documents that will govern the CMIM.
9. We agreed that an independent regional surveillance unit will be established as soon as possible to monitor and analyze regional economies and support CMIM decision-making. As a start, we agreed to establish an advisory panel of experts to work closely with the ADB and the ASEAN Secretariat to enhance the current surveillance mechanism in order to lay the surveillance groundwork for the CMIM. In addition, we welcomed Hong Kong, China, to participate in the CMIM.
10. On **the Asian Bond Markets Initiative (ABMI)**, we stressed the importance of the ABMI in promoting the local currency bond markets and enhancing the recycling of regional savings towards developing regional bond markets. We agreed to enhance the ABMI Roadmap taking into account the outcome of the London Summit.
11. We endorsed the establishment of the Credit Guarantee and Investment Mechanism (CGIM) as a trust fund of the ADB with an initial capital of US\$500 million which could be increased once

the demand is fully met. The objective of CGIM is to support the issuance of local currency-denominated corporate bond in our region. This initiative would contribute to developing regional bond markets. Issues regarding the establishment of CGIM such as business scope, leverage ratio and country limit are to be further discussed at the working level in order to make the mechanism to be effective by the 2010 AFMM+3.

12. In addition, we agreed on the proposed provision of the Technical Assistance from ADB with regard to the pilot project on cross-border infrastructure bond issuance by the Lao government in Thailand. We also agreed to explore the possible measures to enable mutual access to securities markets in the region. We took note of the active efforts and progress made in discussions by the Group of Experts composed of private sector participants, especially on cross-border bond transactions and settlement issues.
13. On **the ASEAN+3 Research Group**, we acknowledged the usefulness of the various studies conducted by the Research Group on financial market development in the region. We endorsed two topics for the 2009/2010 Research Group activities as follows: (1) Ways to Promote Trade Settlement Denominated in Local Currencies in East Asia, and (2) Regulation and Supervision for Sound Liquidity Risk Management for Banks.

Conclusion

14. We expressed our appreciation to the government of Thailand and Republic of Korea for their excellent arrangements as co-chairs of the ASEAN+3 Finance Ministers' Process in 2009. We also thanked the government of Indonesia for its hospitality and kind cooperation.
15. We agreed to meet in Tashkent, Uzbekistan in 2010. China and Vietnam will be the co-chairs of the ASEAN+3 Finance Ministers' Process in 2010.

1. The objectives of Chiang Mai Initiative Multilateralisation (CMIM) are (i) to address the short-term liquidity problem in the region and (ii) to supplement the existing international financial arrangements.
2. The multilateralised arrangement will be governed by a single contractual agreement. The total size of the CMIM is USD 120 billion with the contribution proportion between ASEAN and the Plus Three countries at 20:80. The maximum amount that each country can borrow is based on its contribution multiplied by its respective borrowing multiplier.

Country	Contribution (USD Billion)		Borrowing Multiplier
Brunei	0.03		5
Cambodia	0.12		5
China	38.4	China (Exclude Hong Kong, China) 34.2	0.5
		Hong Kong, China 4.2	2.5*
Indonesia	4.77		2.5
Japan	38.4		0.5
Korea	19.2		1
Lao PDR	0.03		5
Malaysia	4.77		2.5
Myanmar	0.06		5
Philippines	3.68		2.5
Singapore	4.77		2.5
Thailand	4.77		2.5
Vietnam	1.00		5

- Hong Kong, China's borrowing is limited to IMF de-linked portion because Hong Kong, China is not a member of the IMF.

3. On decision-making mechanism of the CMIM, the fundamental issues will be decided through consensus of members of ASEAN+3, while the lending issues will be decided through majority.

	Issues	Rule of Decision-Making
Fundamental issues	Review (size, contribution, and borrowing multiples), Re-admission, Membership, Terms of Lending, etc.	Consensus
Lending issues	Lending ----- Renewal, Default.	Majority