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East Asian Financial Safety Net: The Problem of Leadership

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Synopsis

A core challenge facing the advancement of a regional financial safety net in recent years has been an absence of leadership. Without such clear regional leadership, the future advancement of such a safety net -- Chiang Mai Initiative Multilateralization (CMIM) - would be modest at best.

Commentary

AFTER THE Asian financial crisis, East Asia witnessed regional financial cooperation that has never seen before. The countries' realisation of their economic vulnerabilities coupled with a strong aversion towards International Monetary Fund (IMF)'s assistance during the crisis tempted the policymakers to seek regional "self-help" mechanisms.

The result was the ASEAN+3 financial cooperation process set up in 2000, which established regional financial governance architectures including the Chiang Mai Initiative Multilateralisation (CMIM). Its purpose is to provide short-term liquidity assistance through a network of currency swaps in case of balance-of-payments difficulties.

CMIM: Arrested Development

The CMIM has since evolved. For example, the size of the fund was raised to US$240 billion in 2014. Its IMF de-linked portion, which allows the members to borrow up to a certain percentage of its maximum drawing amount without being put under an IMF programme, increased to 30 percent in 2014.

Moreover, the ASEAN+3 Macroeconomic Research Office (AMRO) -- CMIM's

surveillance arm -- was transformed into an international organisation in 2014. However, its continued development seemed to have been arrested. Neither the size nor the de-linked portion has been expanded since 2014. With its current size of $240 billion, the entity can at best assist a few small-to-medium economies in crisis times.

The current IMF de-linked portion requires a member desiring to draw on more than 30 percent of its maximum borrowing amount to sign onto IMF's structural assistance programmes. This could jeopardise CMIM's objective of disbursing financial support in a timely fashion because getting the Fund's agreement may take time.

Furthermore, critics worry that AMRO and its activities may not be able to completely break free from international politics. This is mainly because AMRO's activities are overseen by the Executive Level Decision-Making Body (ELDMB) comprising ASEAN+3 deputy finance ministries and deputy central bank governors.

Lack of Leadership?

The little progress in recent years has partly been caused by a lack of leadership in the ASEAN+3 financial cooperation process. Leadership is needed to realise international collaboration. Certain states must take a lead in not only championing ideas but also persuading or pressuring the others to get on board. Regarding financial regionalism, the key question is: "Which ASEAN+3 parties would provide leadership?"

The three possible scenarios below are derived from the CMIM weighted voting system. Illustratively, CMIM decisions on executive issues (e.g. financial support disbursement) are governed by a two-thirds supermajority voting system. As far as voting powers are concerned, Japan, China (including Hong Kong), and the ten ASEAN nations hold equal votes of 28.41. Thus, leadership by them is explored.

Also, South Korea's leadership is scrutinised because despite having 14.77 votes, the state possesses power to cast a determining vote when China, Japan, and ASEAN vote on lending decisions differently. For instance, suppose the ten ASEAN countries and China (or Japan) vote to activate lending while Japan (or China) votes against it. Their combined votes constitute only 56.82 (28.41+28.41), which is under the two-thirds supermajority threshold.

To pass this threshold, these states must court Seoul to vote in their favour. Under these circumstances, South Korea becomes a veto power in effect.

Three Scenarios of Leadership

By China-Japan

The first scenario suggests a China-Japan co-leadership. This is more likely than leadership provided by either Beijing or Tokyo due to the power rivalry between them. Also, both countries are likely to have an incentive to co-lead as they are potential lenders and are the biggest CMIM contributors.

Nevertheless, such scenario is unlikely as Beijing and Tokyo are still playing their contestation game. Instead of working together to beef up CMIM, both have

established their own separate bilateral currency swap networks within the region via the People's Bank of China and the Bank of Japan respectively. Therefore, the extent to which Beijing and Tokyo could move beyond their rivalry to jointly lead ASEAN+3 process remains to be seen.

By South Korea

Another scenario is South Korean leadership. Compared to China and Japan, proposals tabled by Seoul is likely to be more well-received by ASEAN participants. It is because unlike the former, South Korea is perceived as a neutral actor with no geopolitical aspirations. Concerning CMIM, the state has never attempted to build up its own bilateral currency arrangement networks which could undermine the mechanism's development. However, the chances of Beijing and Tokyo accepting Seoul's leadership are less clear.

By Southeast Asia

Alternatively, Southeast Asian nations might provide leadership. Despite being lesser powers when compared to their Northeast Asian peers, these states showed that they could bargain as a bloc to increase their clout at several international fora such as the World Trade Organisation (WTO) and Asia-Pacific Economic Cooperation (APEC).

However, this leadership faces certain obstacles. For example, ASEAN parties are potential CMIM borrowers. Such position might erode their influence over the future development of CMIM vis-a-vis their Northeast Asian neighbours which are the likely lenders to this scheme.

In sum, a core challenge facing the advancement of a regional financial safety net in recent years has been leadership, or the lack of it. However, paths for ASEAN+3 stakeholders to play a leading role are confronted with challenges. While Beijing and Tokyo are less likely to jointly lead, the probability of South Korea and ASEAN providing leadership is doubtful. With such a leadership void, the future advancement of CMIM can at best be modest.

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