

**Regional Economic and
Financial Monitoring:
The ASEAN Surveillance
Process**

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Financial Monitoring and Surveillance: The Context

The Asian crisis highlighted the need for reform of the international and domestic financial systems

- Monitoring and surveillance: an integral part of many reforms

Why surveillance at the regional level?

- **Stability is a public good.**
- **Relative paucity of surveillance at regional level in Asia prior to crisis.**
- **Contagion has a regional scope.**
 - **Rapid spread**
 - **Size and volatility of capital flows**
- **Region is a natural “disciplinarian”**

The ASEAN Surveillance Mechanism

- **To complement IMF global surveillance**
- **To induce pre-emptive policy responses at:**
 - National level
 - Subregional level
 - Regional level and/or
 - Global level

The ASEAN Surveillance Mechanism

- **To develop a system that can provide early warning signals for an impending crisis**
- **To induce joint pre-emptive policy responses**
- **Consultation and sharing of experience**

Requisites for achieving the objective

- **A common understanding on:**
 - An analytical framework
 - A menu of policy responses
- **International cooperation in exchange of information: the “ASEAN way”**
- **Policy support and ownership: ASEAN Surveillance Coordinating Unit**
- **Peer pressure incentives for remedial policy actions**

What is the value added of the ASEAN process?

- More is better. What is the cost?
- Too early for a track record.
- Analytical justification: how the process can address the gaps in global and national surveillance.

Why wasn't the crisis spotted? Why surveillance could fail..

- Countries do not disclose accurate and timely information.
- Politics can frustrate adequate policy responses.
- Limitations of the models used.
 - Are crises predictable?
 - Endogeneity of policy
 - New variety of crisis: **All crises are not alike** and so can not be accurately predicted

Indicators (Salvatore model)

- Savings Rate • $< 24\%$
- Budget Deficit • $> 3\%$
- Current A/C Deficit • $> 5\%$
- Foreign Debt • $> 30\%$
- Short-term Debt • $> 10\%$
- C/A Def - FDI • $> 3\%$
- Debt Service (% X)
- Import Cover, months

Suggested indicators (ESCAP):

● Macroeconomic stress

- Fiscal deficit
- Inflation rate
- Real GDP growth or level
- Savings/investment gap
- Employment/unemployment
- Financial market indices
- Government consumption

● Financial stress

- Composition of foreign capital flows
- Interest rates
- Credit growth
- Money supply
- M2/international reserves
- Parallel financial market premium
- Central bank credit to banks/public sector
- Private sector debt

● External stress

- International reserves
- Foreign investment
- Exchange rate
- Trade balance
- Terms of trade
- OECD growth

● Institutional stress

- Exchange rate system
- Risk management measures
- Prudential measures
- Capital adequacy provisions
- Level of non-performing loans
- Measures of transparency
- Independence of Central Bank
- Measures of creditor and property rights

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- Conditions of an economy may be too weak for crisis prevention measures to matter.
- National authorities are unsure of what the problem really is.
- Lack of regional perspective. Regional linkages in the transmission of crisis.

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Gaps and Fillers

- Countries do not disclose accurate and timely information... **Fostering transparency for market discipline.**
- Politics can frustrate adequate policy responses.... **Peer pressure or constructive intervention.**
- Limitations of the models used.... **Policy support from international agencies.**

Why wasn't the crisis spotted? Why surveillance could fail..

- Conditions of an economy may be too weak for crisis prevention measures to matter...facilitate information flow to prevent build up of vulnerabilities.
- National authorities are unsure of what the problem really is.... Consultation and policy support.
- Lack of regional perspective. Regional linkages in the transmission of crisis. ... regional mechanism is a more “natural” disciplinarian.

Scope for regional cooperation

- **All crises are not alike** and so can not be accurately predicted
- Yet, **efforts to set up early warning systems** are worthwhile in view of the large **economic and social costs** of a crisis
- No model of early warning is totally reliable, but some **indicators are useful** for signaling vulnerability
- **Identification of indicators** and initiating **appropriate policy responses** are, therefore, desirable