

APEC FINANCE MINISTERS MEETING

Kananaskis, Alberta, Canada

May 23-24, 1998

JOINT MINISTERIAL STATEMENT

1. We, the Finance Ministers of the Asia-Pacific Economic Co-operation (APEC)¹ forum met in Kananaskis, Canada to assess future prospects for growth and development within our region in light of the Asian crisis and to discuss policies and measures to improve such prospects. The meeting in Kananaskis marked the fifth time this forum has convened.
2. We welcomed Peru, Russia and Vietnam as official observers to our meeting, and look forward to their induction as full member economies in November in Malaysia.
3. Our discussions focussed on two broad themes. The first was an assessment of the current economic situation and policies to restore financial stability and growth, including measures to strengthen social safety nets to help cushion the impact of the crisis on the poor. The second was the development and strengthening of financial markets in the region so as to reduce the likelihood of future financial instability and to facilitate the continued dynamic growth of the region. In this regard, we reaffirm our commitment to doing our part to support the APEC goal of free and open trade and investment by 2010 in developed economies and by 2020 in developing economies.
4. The Managing Director of the International Monetary Fund (IMF), the President of the Asian Development Bank, and the President of the World Bank joined our discussions.
5. We had a constructive dialogue with the APEC Financiers Group and key representatives of the APEC Business Advisory Council (ABAC) and the Pacific Economic Co-operation Council (PECC) on measures to encourage the resumption of private capital flows to affected economies. We also recognized the importance of the Year 2000 problem and urge all the economies in our region to take urgent action to address this issue. We express our appreciation to the panellists who guided discussions in those sessions.

Causes of the Financial Instability in Asia

6. We reviewed key macroeconomic and structural issues in the APEC region. The financial turmoil in Asia over the past year has affected not only the APEC region, but has also been a major source of uncertainty in the world economic outlook generally. In this regard, while there are many distinct causes of the crisis in Asia, we also noted some similarities to the conditions leading up to the financial instability experienced by Mexico and other parts of Latin America in 1994-95, such as large short-term capital inflows, growing current account deficits as well as inadequate banking supervision and regulation.
7. In the decade leading up to the Asian crisis, generally prudent macroeconomic policies had contributed to strong economic growth in most of the Asian economies. During the mid-1990s, however, signs of overheating emerged as high investor confidence and ready access to capital fuelled excess domestic demand in some economies. This contributed to asset market inflation and large current account deficits, which were financed by large capital inflows from developed economies. These inflows placed strains on policy and institutional frameworks that, in the end, proved excessive for some economies.

¹ Australia; Brunei Darussalam; Canada; Chile; China; Hong Kong, China; Indonesia; Japan; Korea (Republic of); Malaysia; Mexico; New Zealand; Papua New Guinea; Philippines; Singapore; Chinese Taipei; Thailand; and the United States.

8. In retrospect, some economies clung too long to an unsustainable and incompatible mix of exchange rate and monetary policies, even after signs of vulnerability had emerged. In those cases, rigid exchange rate arrangements and close ties to the U.S. dollar limited the ability of monetary policy to control overheating pressures and encouraged foreign borrowing by the private sector, often at short maturities. The combination of these factors contributed to an excessive accumulation of short-term, unhedged foreign-currency-denominated debt. Inadequate supervision and corporate governance, particularly in the financial sector, inadequate intermediation of foreign and domestic savings, and government-directed lending also contributed to inefficient investment.
9. At the same time, strong growth masked existing structural problems, including in the financial sector. Rapid cross-border capital flows in a globalized and integrated financial market also introduced new challenges for macroeconomic management and rendered some of these economies vulnerable to adverse external developments, especially sudden reversals in market sentiments.
10. In 1997, these problems became more apparent as a result of a number of developments in the major industrialized economies, including a weakening in import demand, particularly for key export products from the Asian region. The U.S. dollar's rise in value against major currencies may have also played a role in a loss of competitiveness of the region's exports.
11. Although the situations of individual economies varied across the region, instability tended to spread to economies that markets perceived to have similar vulnerabilities. In some cases, a lack of transparency in financial systems contributed to these market perceptions. We also note that in some cases markets did not appear to differentiate appropriately on the basis of available information about the economic fundamentals of these economies.
12. We agreed that speculation in financial markets was not the root cause of the turmoil, although it may have played a role in exacerbating herding behaviour and spreading volatility. We took note of the useful work done by the IMF in its study "Hedge Funds and Financial Market Dynamics." We agreed to keep these issues, including the role of institutional investors and their investment behaviour, under consideration in our future meetings, with contributions as appropriate by the IMF.
13. In our discussions, we focussed on two dimensions of the response to the recent turmoil. The first was the challenge of restoring stability and promoting recovery in the affected economies. The second involved reinforcing our financial systems, and indeed the global financial system, so as to reduce the likelihood of future recurrences.

Restoring Stability and Promoting Recovery

14. We acknowledge the crisis is a global problem with regional manifestations. In reaffirming the central role of the IMF, we echo our APEC Economic Leaders call in Vancouver regarding the Manila Framework for Enhanced Asian Regional Co-operation to Promote Financial Stability, and we welcome developments that support that call, including the formation of regional economic surveillance mechanisms.
15. We endorse the approach of the IMF, the World Bank and the Asian Development Bank in addressing the financial instability in Asia. We applaud the efforts of these multilateral institutions and bilateral donors to provide valuable financial and technical assistance to Thailand, Indonesia and Korea to help them meet the numerous challenges they face including corporate and financial restructuring, balance of payments difficulties, trade financing needs and the severe social effects of the recent financial turmoil. We welcome the IMF's creation of the Supplemental Reserve Facility, to help address problems posed by sudden changes of market sentiment toward individual or groups of economies. We also welcome the enhanced financial resources provided by the Japan Special Funds, at the World Bank and the Asian Development Bank, and the ASEM trust fund, at the World Bank, for assisting economies in dealing with the effects of the recent crisis.

16. We call for the early ratification of the increase in quotas approved by the Board of Governors in January 1998 and of the New Arrangements to Borrow in order to ensure that the IMF has adequate resources to respond to any spread or intensification of the current crisis and to handle future crises.
17. We commend those economies in the Asian region that have taken difficult and courageous measures to deal with the causes of the instability. We welcome signs of improved prospects in Thailand and Korea as implementation of their IMF-supported economic programs has progressed. We expressed deep concerns about the recent economic and social situation in Indonesia. We welcome the new President's support for political and economic reform and his commitment to implement the recently-strengthened IMF-supported program. We look forward to progress toward economic and political conditions that will permit the restoration of confidence that is essential for recovery. Overall, the long-term fundamentals in the region remain strong and we are confident that the region will regain its dynamism. We agree, however, that there is no room for complacency as difficult adjustments and challenges remain.
18. We note the continuing importance of long-term capital flows, particularly foreign direct investments, for growth in the Asian region. We discussed this in our joint session with the APEC Financiers Group and concluded that a sustained resumption will require not only a stabilised macroeconomic and exchange rate environment, but also significant reforms in the corporate and financial sectors and improvements in the transparency of market arrangements. We have also noted that those economies that have undertaken these reforms earlier have been able to weather the crisis better and maintain investor confidence. The Philippines, for example, was the first Asian sovereign borrower to tap the international capital markets after the onset of the financial turmoil in Asia. Korea and Thailand, which have shown their steady and strong commitment to reforms, have seen improvements in the value of their currencies and have recently returned to international capital markets.
19. The recent instability has, however, left financial sectors in the region severely weakened, with a large stock of non-performing loans and an increased burden of foreign currency debt. Forceful action to restore health to domestic financial systems in many economies is clearly vital for the resumption of capital flows and growth. We endorse the work the World Bank and the Asian Development Bank are carrying out in supporting the affected Asian economies to reform and strengthen their financial systems and promote sound corporate restructuring.
20. We especially took note of the social impact of the turmoil and the adjustment policies necessitated by it. In the coming months, as companies restructure, the level of unemployment in a number of economies may rise even further. The situation is placing strains on the social fabric and the burden in many cases falls on the poorer segments of society and those least able to protect themselves, especially women and children. In Indonesia there is even evidence of food shortages and inadequate medical supplies.
21. These problems make it important to expand and strengthen social safety nets and other forms of support that exist in these economies. In this regard, we applaud the efforts of the ADB and the World Bank to date to help the affected economies deal with the social impact of the turmoil. We also recognized the flexibility that the IMF has shown in adapting its program requirements to changing economic and social circumstances in the region. We urge these institutions to continue to look for innovative ways of offering support for those hardest hit by the instability.
22. It will also be important for international financial institutions to consider ways to support environmental protection in these economies as they respond to the crisis.
23. We welcome the efforts by those APEC economies less affected by the instability to support economies' prospects in the region as a whole by pursuing policies that promote domestically-led growth. We commend those APEC economies that have demonstrated their policy commitment to maintain stability of their exchange rates, thereby helping to restore confidence in this region. We encourage all economies to maintain movement towards open markets. In this context, as called for by APEC Economic Leaders in Vancouver, we appreciate efforts by other APEC fora towards early voluntary sectoral liberalization, in the areas on tariffs, non-tariff measures, trade facilitation, and economic and technical co-operation.

24. We recognized that adequate access to trade financing is imperative to allow industries to import needed inputs to facilitate the recovery of domestic production. In this regard, we welcome efforts by the OECD and regional governments to maintain and expand existing official export financing programs designed so that economies undertaking IMF-supported adjustment programs do not experience unnecessary disruptions in their trade flows. We encourage the ADB and the World Bank to look for appropriate ways in which they may support the restoration of financing for small- and medium-sized companies in affected economies, as the ADB is already doing in Thailand through the use of credit enhancements. We strongly urge our private sectors to base their assessment of individual banks' credit-worthiness on the relevant facts and not on any simple regional formula. In addition, we noted that the private sector (both creditors and debtors) should be encouraged to play a greater role in the resolution of financial crises.

Developing and Strengthening Financial Markets

25. The recent financial instability in Asia underscores the importance of developing strong, resilient and well-regulated domestic financial markets in the framework of a stable international financial system. In this regard, we welcome and endorse the Basle Core Principles on Effective Banking Supervision and urge the International Conference of Banking Supervisors to endorse them at their meeting in October. We endorse the working party report on Financial Stability in Emerging Market Economies prepared by the G-10 in collaboration with a number of emerging market economies. We also noted the efforts of the Asian Development Bank in evolving "Sound Practices to Facilitate Development of the Financial Sectors in the APEC Region" that reflect the lessons of the financial instability in Asia. In the same vein, we also look forward to the results of IOSCO's current efforts to develop an appropriate set of principles for supervision of securities markets.
26. We strongly endorse the idea of enhancing surveillance of financial sector supervisory regimes. We look forward to the international financial institutions and the international regulatory community working together to study ways in which this can be accomplished including options for better co-ordination or enhanced forms of collaboration, such as a peer review process. Any reform should strengthen or complement rather than duplicate existing global or regional arrangements.
27. We welcome the successful completion of the World Trade Organization's Financial Services Negotiations. This agreement will achieve improved market access and lower barriers among financial markets. Greater competition in the provision of financial services can, if the prudential regulatory framework is in place, contribute to capital market development. We urged participating economies to ratify their commitments so that the agreement can enter into force as scheduled on March 1, 1999.

Work in the APEC Finance Ministers' Process on Developing and Strengthening Financial Markets

28. Promoting the development of strong, resilient financial sectors in our region has been a central goal of the APEC Finance Ministers' process since its inception. Our work over the past year has continued to focus on this objective, which has assumed even greater importance in light of the financial crisis in Asia. At our meeting last year in Cebu, we launched six collaborative initiatives to promote capital market development and facilitate private investment in infrastructure projects as a response to our Economic Leaders' call for a concrete and practical work program. We also agreed that our Deputies would prepare a voluntary action plan to support the freer and stable flow of capital in our region.
29. This year in Kananaskis, we discussed and welcomed the progress achieved so far under the initiatives launched in Cebu. We plan to continue our efforts over the next year in three priority areas: capital market development; capital account liberalization; and strengthening international financial systems. Further details of the initiatives and their recommendations are in Annex A.

Capital Market Development

30. Over the past year, we examined ways to further capital market development under a number of collaborative initiatives. We examined ways to strengthen clearing and settlement infrastructure within our economies. On this initiative a final report has been issued to us.
31. We conducted a regional forum on pension fund reform, which produced a very useful technical report on the issue including the role pension funds can play in mobilizing private savings and broadening the demand base for long-term debt instruments. In the next year, Chile will host a second forum, to be co-ordinated by Chile and Mexico, which will focus on policy issues in this area.
32. Under our initiative on securitization, participating economies drafted recommendations on supporting the development of asset-backed securitization, including a voluntary action plan which interested individual economies can implement to support the development of securitization in their markets. We endorse these recommendations.
33. We recalled that the impetus for much of our work on developing and strengthening capital markets was to facilitate private financing of infrastructure. Over the past year, we have continued our work on this subject through our initiative to support co-operation among export-financing institutions. In particular, we welcome the protocol agreement signed by fifteen Export Financing Institutions and Export Credit Agencies from across the region which will provide a framework for co-operation among them when market demand for infrastructure recovers.
34. We recognized, however, that the recent period of financial instability has significantly changed the circumstances for financing infrastructure projects. There is a need to analyze the impact of this on infrastructure development in the region and to explore strategies to promote private financing for infrastructure over the medium term. We call upon the Asian Development Bank to work in this area and to report back to us at our next meeting.
35. We received a progress report on the collaborative initiative to support the development of credit rating agencies and strengthening of information disclosure standards, and look forward to further results next year.
36. We agreed to begin work on a new collaborative initiative on the development of domestic bond markets in the region, which will be co-ordinated by Hong Kong, China. This should be able to build on the contributions on this subject from the APEC Financiers Group.

Capital Account Liberalization

37. We agree to continue to implement policies to enable economies to benefit from and minimize the risks of capital account liberalization. We reaffirm our commitment to continue working on designing a Voluntary Action Plan For Supporting the Freer and Stable Flow of Capital.
38. We recognize that economies should pursue capital account liberalization in an orderly manner. Prerequisites include sound macroeconomic policies, effective prudential regulation and supervision, and an active effort to promote capital market development. Some of our economies have also found the use of market-based prudential safeguards to be a useful complement but not a substitute for these preconditions. We asked our Deputies to work with the IMF and the World Bank to compare the experiences of economies in managing the capital market liberalization process, including the results from the use of macro-prudential measures, in order to study how to promote freer flows of capital while maintaining macroeconomic and financial stability. We asked for a report at our next meeting.
39. We asked our Deputies to work with the IMF to examine how to monitor effectively capital flows, including short-term capital flows, with a view to providing information to the market and promoting stability.

Strengthening Financial Systems

40. Under our initiative to Strengthen Financial Market Supervision, two action plans were developed for strengthening training of bank supervisors and securities regulators in APEC economies. We

endorse these plans and call for their timely and comprehensive implementation. We thank the Asian Development Bank for its assistance in developing these plans and for its commitment, together with that of the South East Asian Central Banks Research and Training Centre (SEACEN) and the Asia-Pacific Regional Committee of IOSCO, to assist in their implementation. We look forward to receiving a progress report at our next meeting.

41. We welcome other training initiatives launched within our own region: the joint initiative of Canada and the World Bank to establish the Toronto International Leadership Centre for Financial Sector Supervision; the opening of the ADB Institute in Tokyo; the IMF-Singapore Regional Training Institute (STI); and bilateral training assistance provided by individual economies.
42. We welcome the initiative of the APEC Financiers Group to create a private-sector training and education program for financiers across the APEC region. We call on our APEC Deputies to work actively with the financiers on this initiative and look forward to a status report.
43. As part of our efforts to draw lessons from the recent crisis and strengthen our economies, we agreed to launch an initiative to be co-ordinated by Malaysia in conjunction with the World Bank and the Asian Development Bank, to examine ways of strengthening corporate governance in our region. This work would recognize work going on in other fora. As part of this initiative, we welcomed Australia's offer to host a seminar to bring together senior business people from our economies to identify priorities for reform in this area. We look forward to reviewing a report on this subject at our next meeting.

Other Matters and Future Meetings

44. We welcome the progress made by the Sub-Committee on Customs Procedures (SCCP) in their twelve-point collective Action Plan to facilitate trade in the region. The "Blueprint for APEC Customs Modernization" and the "Guidelines for SCCP and Business Strategic Partnerships" are important contributions for strengthening co-operation with the business community. Reaffirming that trade facilitation and enforcement must be well co-ordinated, we encourage customs authorities to continue strengthening such co-operation.
45. We also encourage our officials to expand coverage of bilateral tax treaties with appropriate economies in the region in conformity with international norms and to continue the useful dialogue on taxation through APEC-OECD joint symposia of tax officials. We look forward to the results of the next APEC-OECD tax symposium in Manila.
46. We reaffirm our appreciation to the APEC Financiers Group for their ongoing participation in the APEC Finance Ministers' process. We had a very useful discussion with the Group on the importance of implementing the necessary measures to resolve in a timely manner Year 2000 problems in our economies. We urge the World Bank and the ADB to help economies to address this issue. We call on the supervisory and regulatory authorities in our economies to work with one another, and with the Basle Committee on Banking Supervision, IOSCO, and the IAIS as they review and monitor Year 2000 compliance efforts by all financial institutions.
47. We would like to thank the people and Government of Canada and the Department of Finance for the hospitality extended to all the delegations and the excellent arrangements they have made to make the fifth APEC Finance Ministers Meeting a success. We also thank the chairman of the APEC Finance Ministers Meeting, the Honourable Paul Martin, for his valuable contribution to the success of this meeting.
48. We look forward to the next meeting of APEC Finance Ministers in Penang, Malaysia.
49. Finally, we will report to the APEC Economic Leaders on the outcomes and recommendations of this APEC Finance Ministers Meeting and on any subsequent and related matters, on the occasion of their next meeting in Malaysia in November.

Regional Forum on Securitization: Although securitization is fast becoming an important source of financing, many structural, regulatory, fiscal and other obstacles continue to inhibit its further development. In an effort to begin to address these obstacles, an international conference on securitization and a workshop for regulators from within the APEC region were held in Kuala Lumpur, Malaysia last December. A survey on the status of securitization activities in APEC member economies was carried out to gather information on these activities in APEC economies and to identify pertinent developmental issues and regulatory concerns. Based on the outcome of these activities, we encourage the development of securitization activities through (i) the continued removal of impediments to market development; (ii) enhanced training and technical assistance to facilitate the removal of impediments to market development; and (iii) the continued sharing of expertise among our economies. We have adopted a voluntary action plan to assist individual member economies that are interested in accelerating the development of securitization activities in their own markets.

Regional Forum on Pension Fund Reform: Officials from many of our member economies, together with academics and experts from the IFIs, attended the Regional Forum that was held from February 4-6 1998, in Cancun, Mexico. The forum had as overall objectives the interchange of expertise, information and best practices of pension systems across the APEC region, and the discussion of: the lessons of Latin American pension reforms for APEC economies; the potential for reform and its impact on the development of financial markets, domestic savings, and income distribution; the strategies for the administration of pension funds; the prudential regulation of pension funds investments; and the relative role of the private and the public sectors in pension fund management. A background report describing the pension systems of the APEC economies and outlining the major issues and difficulties was prepared by the ADB.

We recognized that pension funds can play an important role in mobilizing private savings, and broadening, together with other institutional investors, the demand base, especially for long-term debt instruments. Moreover, permitting pension funds to invest in financial instruments other than low-income government bonds can greatly enhance the supply of long-term finance to the private sector. We also recognized that factors such as ageing populations, low levels of national savings, unsustainable pressure on public finances and distortions created by high social security contributions make pension fund reform a priority for many APEC economies, placing it at the top of the economic and social agenda. While pension reforms can be spread along a broad spectrum, a sound prudential and regulatory framework is necessary for all types of public and private pension schemes.

Strengthening Financial Market Supervision: Recognizing the importance of sufficiently trained financial supervisors, we assessed the adequacy of existing training programs for both bank supervisors and securities regulators. We identified significant unmet training needs and limitations in the training management process at the domestic level, and determined that enhanced regional and international co-ordination to address these concerns would be useful. Importantly, we recognized that improvements in training programs would only be effective in enhancing the quality of supervision where a sound supervisory and regulatory regime is in place, and that training programs should be based on sound supervisory and regulatory principles.

Based on these results, we agreed to implement in a timely and comprehensive manner the Action Plans for Strengthening Training of Bank Supervisors and Securities Regulators in APEC economies. The Action Plans include measures to improve the quality of training programmes at the domestic level and to strengthen co-ordination in meeting training needs through regional and international programmes. Regional advisory groups will be established to oversee the implementation of the Action Plans, while the day-to-day responsibilities will be overseen by a secretariat to be funded and located at the ADB. We thank the ADB for its valuable assistance in implementing the Action Plans and for funding the secretariat and the technical assistance requirements of both plans.

Enhanced co-operation among export financing institutions: Export financing institutions (EFIs) can play a catalytic role in mitigating risks and mobilizing private-sector financing for infrastructure development. Representatives of the Export Financing Institutions (EFIs) in the APEC region have met several times to discuss the role of EFIs in promoting private sector infrastructure projects, including the opportunities for co-operation among EFIs through information exchange, knowledge

transfer, possible co-lending, and the opportunity for policy dialogue between EFIs and host economies.

EFIs also discussed their role in the wake of the Asian financial instability as an important example of EFI co-operation. We recognize different mandates and approaches in various EFIs, however we expect a synergy effect through their co-operation. In view of strengthening EFI co-operation, we also welcome the protocol agreement which sets out a framework for promoting technical co-operation and has been signed by fifteen EFIs and Export Credit Agencies from across the region.

Supporting the development of credit rating agencies and strengthening information

disclosure standards: We encourage the development of independent rating agencies according to international best practices. In order to assess the status of existing rating agencies we examined the current experiences with credit rating agencies in the region to determine how well they are fulfilling their key role in promoting the flow of timely and accurate information across capital markets. The results of work completed thus far include the identification of some of the important issues to be addressed, some of which pertain to the scope for harmonization and increasing the transparency of credit rating agencies' activities. We are currently examining experiences in the region regarding credit rating services. We hope to identify ways to improve rating agencies' ability to promote the flow of timely and accurate information to capital markets. We also encourage steps to strengthen information disclosure standards in the region consistent with international best practices.

Strengthening clearing and settlement infrastructure: Modern clearing and settlement systems are integral to capital market development. The ADB and several member economies stand ready to provide technical assistance to help strengthen clearing and settlement systems in economies with less advanced systems. We welcome the report of the Executive Meeting of East Asian and Pacific Central Banks (EMEAP) in this area.