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## **ASEAN+3 Regional Financial Safety Net and IMF: Time for Structured Cooperation**

*By Pradumna B Rana*

### **Synopsis**

*The regional financial safety net (RFSN) that the ASEAN+3 countries have been establishing during the last two decades can only be successful if it evolves into a more structured form of cooperation with the IMF.*

### **Commentary**

THIS WEEK marks the 20th anniversary of the Asian financial crisis (AFC). The turmoil began in Thailand on 2 July 1997 and quickly spread to Malaysia, the Philippines, South Korea and Indonesia. The contagion effects of the crisis reverberated around the world. Financial markets collapsed and economic growth rates dipped sharply especially in the five crisis-affected countries.

The social costs of the crisis were also high as poverty levels swelled. Post-crisis recovery turned out to be V-shaped reflecting a sharp fall and a quick rebound and therefore the resilience of the East Asian countries. The AFC highlighted the weaknesses of an international monetary system where the International Monetary Fund (IMF) was the sole crisis-fighter. In East Asia, the IMF had also misdiagnosed the crisis and prescribed wrong policies that deepened the crisis.

### **ASEAN+3 RFSN**

The ASEAN+3 – the ASEAN 10 plus China, Japan and Korea - therefore, decided to establish a “self-help and support mechanism” or a regional financial safety net (RFSN), the centrepiece of which was the Chiang Mai Initiative (CMI) bilateral swaps among the central banks of the member countries. A network of six bilateral swap agreements amounting to US\$84 billion was established.

These swaps were to “supplement existing international facilities” and the way that this complementarity was promoted was by requiring the existence of an IMF-supported programme to provide assistance in excess of a certain percentage of maximum access. Initially, only 10% of maximum access, an ad hoc level, was readily available with the remaining 90% linked to an IMF programme.

The CMI bilateral swaps were not used by East Asian countries in 2009 when the region experienced a severe credit crunch because of the global financial crisis. In fact, Korea and Singapore opted instead to draw on their swaps with the US Federal Reserve. This was because the CMI swaps were small in amount, and the region lacked a surveillance capacity and did not have a rapid response mechanism to trigger the swaps.

### **Strengthening ASEAN+3 RFSN**

Subsequently, the ASEAN+3 took a number of steps to further strengthen its RFSN. It multilateralised the bilateral swaps so that funds could be withdrawn with one contract. The size of the crisis fund, awkwardly named the Chiang Mai Initiative Multilateralisation (CMIM), was also increased to \$240 billion. The ad hoc delinked portion was increased to 30% with a view of eventually increasing it further to 40%.

The decision-making process and operational guidelines were agreed and issued. Finally, the ASEAN+3 Macroeconomic Research Office (AMRO) was established as an independent surveillance unit for the CMIM. The AMRO became an international organisation in February 2016. Are these actions adequate to stem the next financial crisis in the region? Probably not.

Under the CMIM, five ASEAN members – Indonesia, Malaysia, Philippines, Singapore, and Thailand – can borrow a maximum amount of approximately \$23 billion each from the CMIM with an IMF programme in place – one-third of which will be the delinked portion – under a single contract at one go. These amounts are large compared to the old CMI swaps, but still inadequate to prevent and manage the newer types of capital account crisis associated with large inflows and sudden withdrawal of financial capital.

Also important is the speed and efficiency with which requests for assistance can be disbursed. The operational guidelines for the CMIM note that a decision based on two-thirds majority are to be made within two weeks of the swap request. This is unlikely to happen as the CMIM is not a centralised fund, but a “self-managed” arrangement where contributions are held by individual central banks and monetary authorities. Also the decision rests with a non-resident body.

### **The Next Steps**

What can be done to ensure that the ASEAN+3 RFSN is effective in protecting the region from the next crisis? Instead of the ad hoc form of cooperation between the ASEAN+3 RFSN and IMF that exists at present, the two institutions should promote a more structured form of cooperation between themselves. In designing joint

programmes, however, the recent European experience suggests that there should be a clear agreement among institutions in areas of involvement before a crisis hits.

Three cooperative areas between ASEAN+3 RFSN and IMF should be considered. First, ASEAN+3 countries seeking financial resources should be required to apply simultaneously to both the IMF and CMIM and the IMF and AMRO should jointly analyse and evaluate the applications. The advantages of this would be two-fold: Experts from outside East Asia would support an understaffed AMRO; joint application would help address the IMF stigma in Asia which had originated from the feeling of being unfairly treated and being forced to accept inappropriate IMF conditions.

The second area of cooperation should be joint monitoring and surveillance, and conditionality. The two institutions should focus on their relative comparative advantages – the IMF on macro and micro financial and cross regional experience and the AMRO on regional financial and capital market developments and structural reforms. Pooling their resources together through joint IMF-AMRO missions and analysis including conditionality would strengthen the surveillance mechanism.

The third area of cooperation should be co-financing and joint supervision of liquidity provision programmes. Co-financing between the two institutions would increase the resources available to deal with a crisis as has been the case in Europe.

### **“Marriage of Convenience”**

In recent years, the IMF stigma that emerged following the Asian Financial Crisis of 1997 has been declining in the region and the IMF is invited to the ASEAN+3 surveillance meetings. The IMF has also engaged in dialogues with AMRO as part of its outreach activities, although it does not have a formal technical assistance programme.

These engagements should be deepened by the signing of a Memorandum of Understanding between the two institutions for a more structured form of ASEAN+3 RFSN and IMF cooperation as outlined above. Such cooperation would be a “marriage of convenience” for both institutions.

The IMF should not reject the offer as such a rejection would give the impression that the IMF is too euro-centric, which would refuel the lingering stigma of the institution in Asia.

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