



## Competition in the financial sector and its impact on financial intermediation

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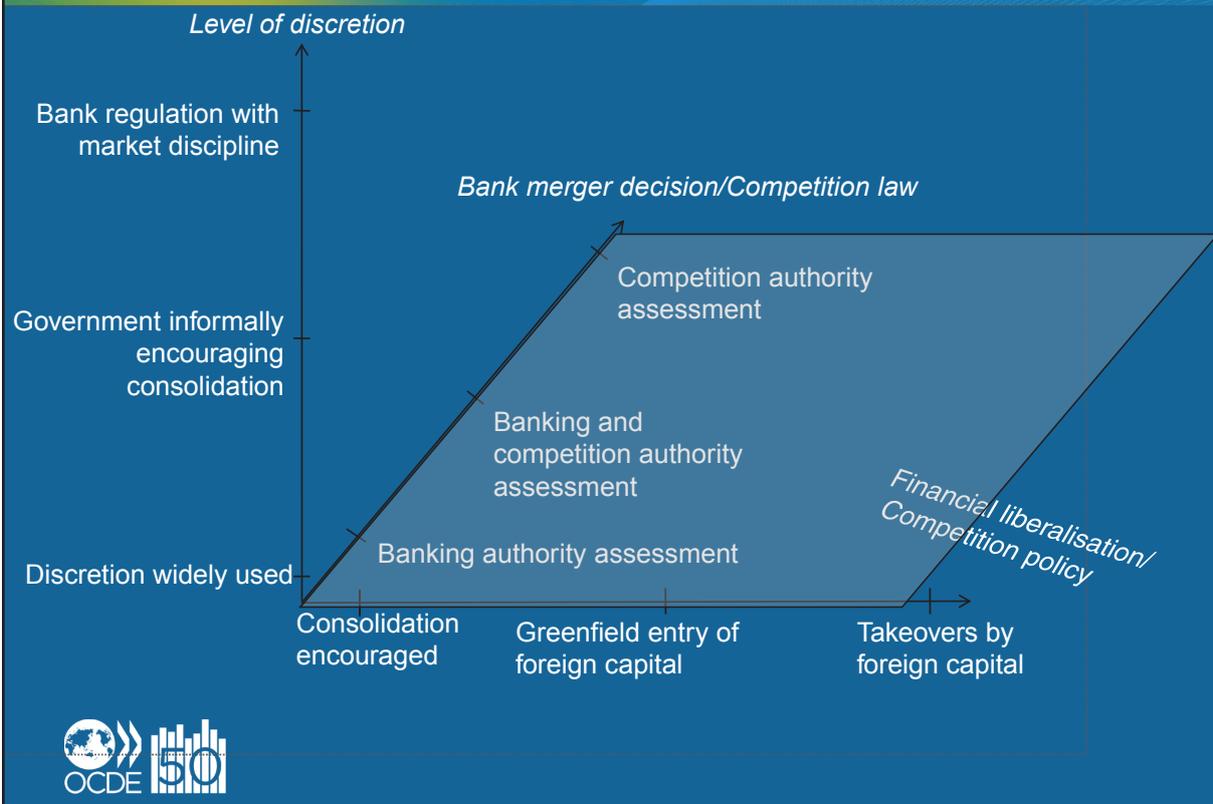
### Evolution of competition policy in the financial sector

- Support and proliferation towards liberalisation and the market economy has brought about the need for the financial sector to consider its competition policy.
- Traditionally, the financial sector was segregated from the competition policy regime maintaining a special status as a heavily regulated industry.
- However, as market economies began to embrace competition, competition policy has become one of the main pillars of banking regulation and supervision.
- Banking and insurance sector have been subject to greater competitive restrictions than securities, historically speaking due to prudential and consumer protection reasons.
- Inherent tension because authorities have a desire to strengthen their financial sector, while financial institutions tend to grow through mergers leading to possible oligopolistic structures.

• Source: Yokoi-Arai & Kawana, Competition Policy in the Banking Sector in Asia (November 2007)  
<http://www.fsa.go.jp/frtc/seika/discussion/2007/20071204-1.pdf>



# Where should the discretion of the regulator be?



## Overview of competition policy elements in the Asian financial markets

	Anti-trust law	Authority for merger regulation	Discretion of authorities on mergers
Japan	O	FSA and Fair Trade Commission	Administrative guidance, financial penalties
PRC	O	Respective supervisory agency	Actions can be taken for prudential concerns
Korea	O	FSC and Fair Trade Commission	Discretionary power related to exemption from shareholding limits
Indonesia	O	Central bank and competition authority discuss informally	Authority to make recommendations on mergers
Malaysia	X	Central bank	Administrative guidance
Philippines	X	Central bank	Administrative guidance
Thailand	O	Central bank	Administrative guidance
Vietnam	O	Central bank	Discretion can be made to specific transaction details
India	O	Central bank	Public interest and necessity taken into consideration



## Overview of competition policy elements in the Asian financial markets

	Foreign capital entrance requirements	Masterplan for greater competition	State-owned bank
<b>JP</b>	Under sufficient supervisory authority in home country	X	X
<b>PRC</b>	Minimum deposit for clients, and gradual easing towards subsidisation	X	4 mega state banks
<b>KR</b>	100% of bank shares can be held by foreign capital	X	Uri financial holding companies (78% government held)
<b>Indo</b>	Foreign capital permitted to hold up to 99% shareholding	Pakto 2006, improvement of prudential standards of banks. ASEAN Economic Community Blueprint	4 state held banks
<b>Malay</b>	Subsidiaries only	Islamic banking is being developed and expanded, Financial sector masterplan. New masterplan being drafted. ASEAN Economic Community Blueprint	X
<b>Philip</b>	Up to 60% of shareholding by foreign capital	Act liberalizing the entry and scope of operations of foreign banks ASEAN Economic Community Blueprint	X
<b>Thai</b>	Branching and subsidiaries. Thai financial institutions, 75% voting shares and directorship to be Thai.	Financial sector masterplan ASEAN Economic Community Blueprint	Nationalisation of problem banks
<b>VN</b>	Branching, and joint ventures. Foreign bank branches required to lend against own chartered capital, instead of parent from 2010.	With the WTO accession, Financial Sector Vision ASEAN Economic Community Blueprint	4 mega state banks
<b>India</b>	Joint ventures	1991, 1998, Narashiham Commission Reports Draft Guidelines for licensing new banks in the private sector (Aug 2011)	State bank of India and 17 other banks state held

## Recent turn of events in Asia

- India: new entrants to banking sector, foreign investors to be allowed to take direct stakes in listed companies
- China: opening of off-shore renminbi to purchase onshore equities
- Thailand: permission of foreign bank for greater domestic branching
- Vietnam: insurance law bill recognising cross-border provision of insurance and branching.
- ASEAN Economic Community Blueprint implementation by 2015

## Issues resulting from restrictive or vice versa measures

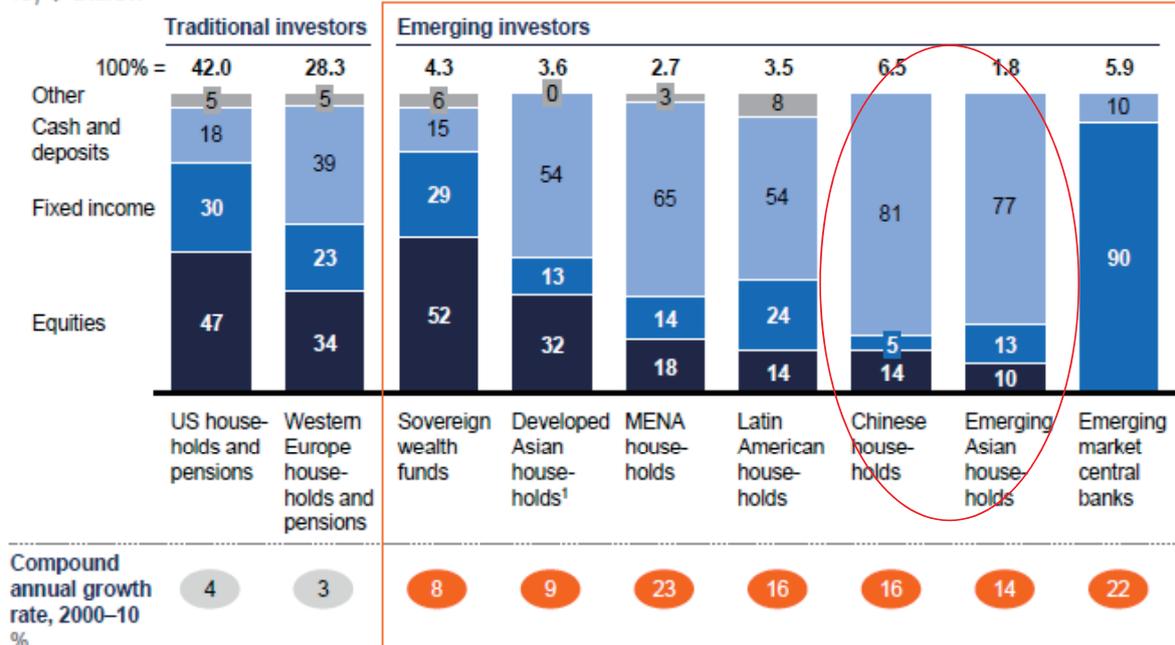
- Russia: insurance sector has 25% quota on total foreign capital holding shares. When a new minimum capital standard was introduced, many foreign based insurers were unable to meet the requirement, due to the quota being used by domestic insurers who were round-tripping capital from Cyprus where there is a tax agreement.
- Too big/important to fail concerns are widely held, particularly, in the banking sector. This will affect attitudes toward G-SIFIs in emerging markets, as their franchise value may not be as high as previously considered.
- Market liberalisation may lead to vulnerabilities, in particular, from capital flows.



## Investors' asset allocation

Asset allocation by investor, 2010

%; \$ trillion



<sup>1</sup> Includes Singapore, Hong Kong, Korea, and Taiwan. Excludes Japan, where households allocate 10% of their portfolio to equities.

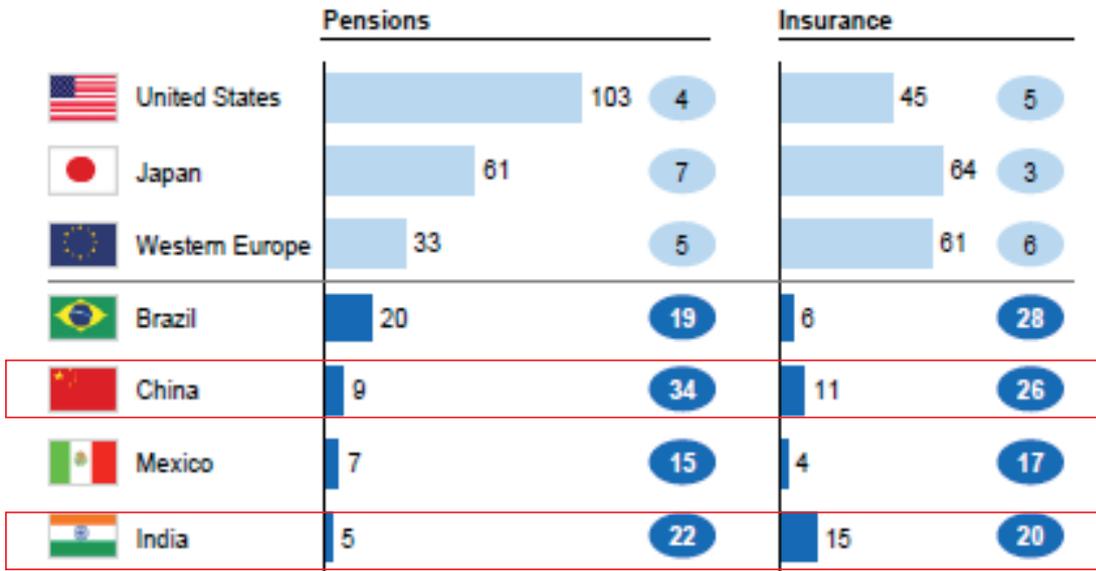
SOURCE: National sources; McKinsey Global Institute

# Pension and insurance market potential

## Emerging markets' pension and insurance industries are still small

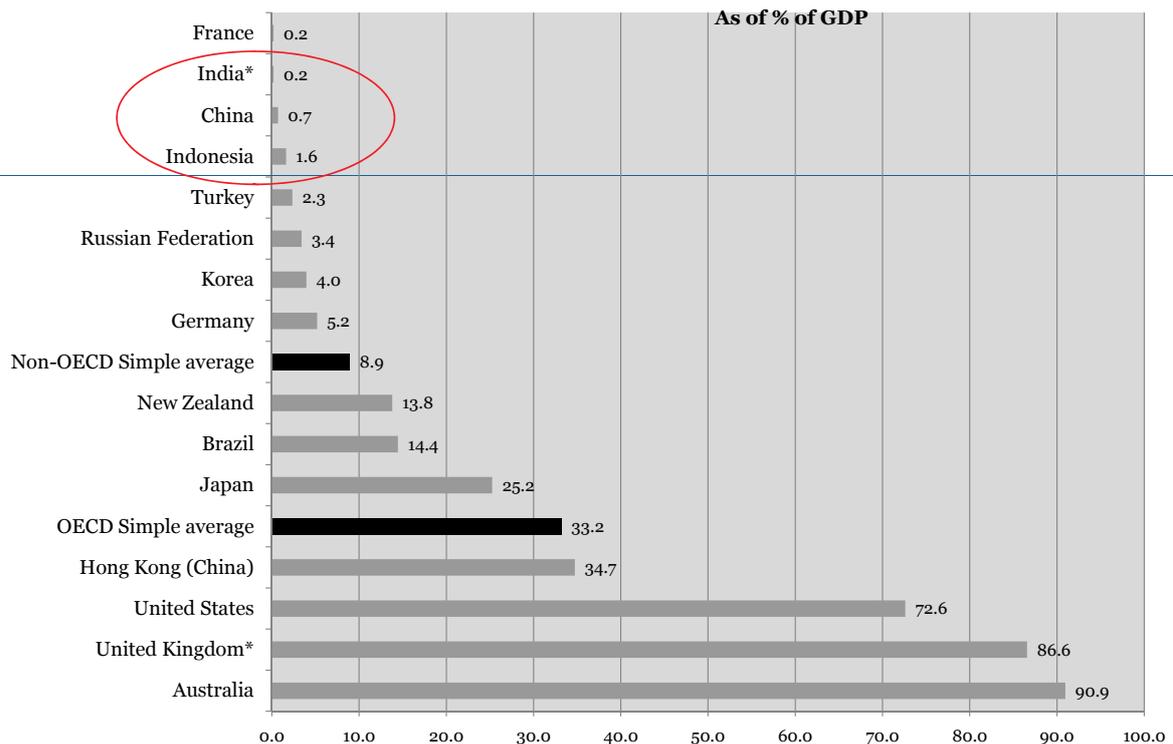
Institutional investors' total financial assets, 2010  
% of GDP

■ Developed countries  
■ Emerging markets  
○ Compound annual growth rate, 2000-10 (%)

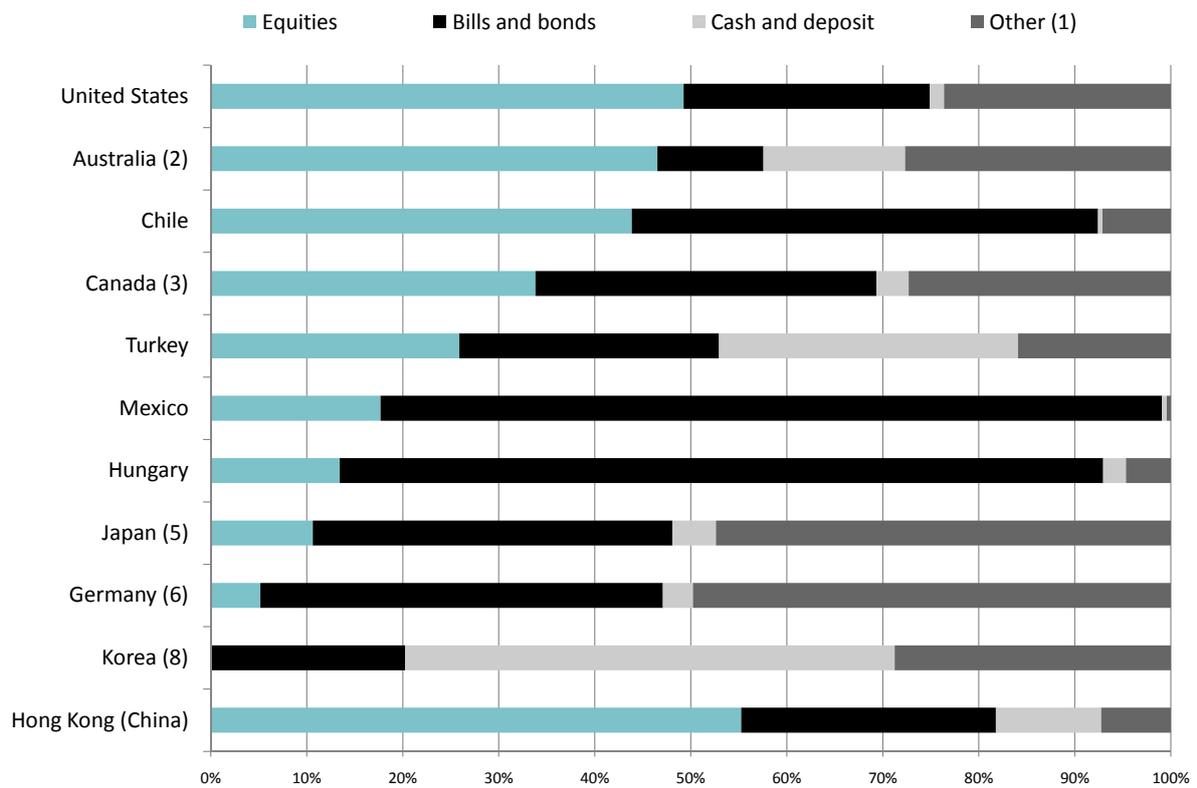


SOURCE: National sources; McKinsey Global Institute

# Importance of pension funds relative to size of economy

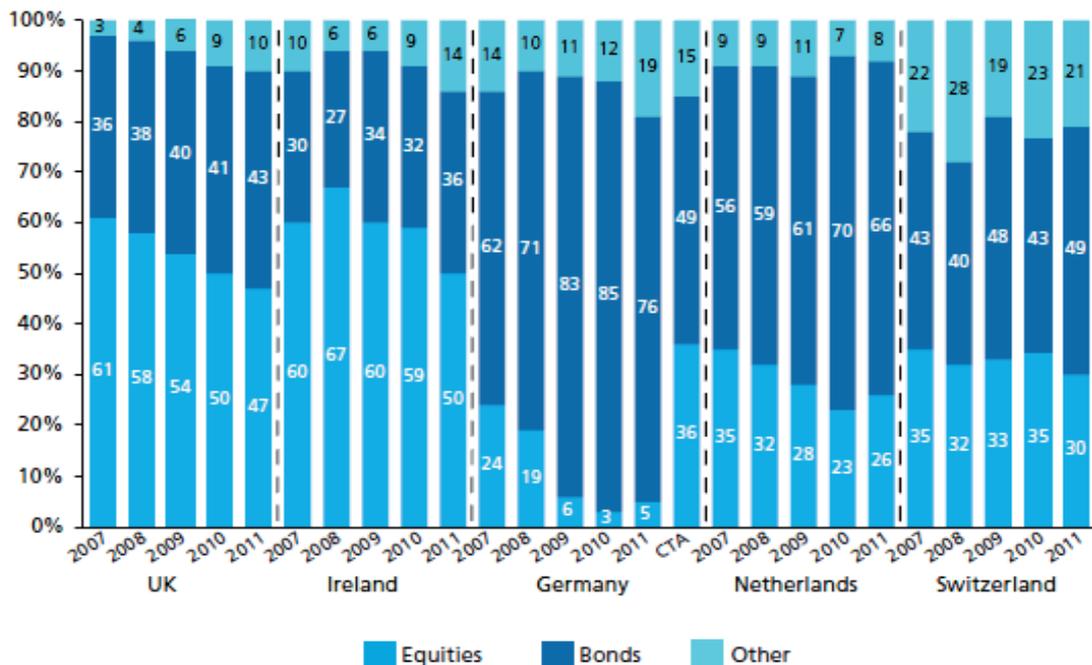


## Pension fund allocation for selected investment categories

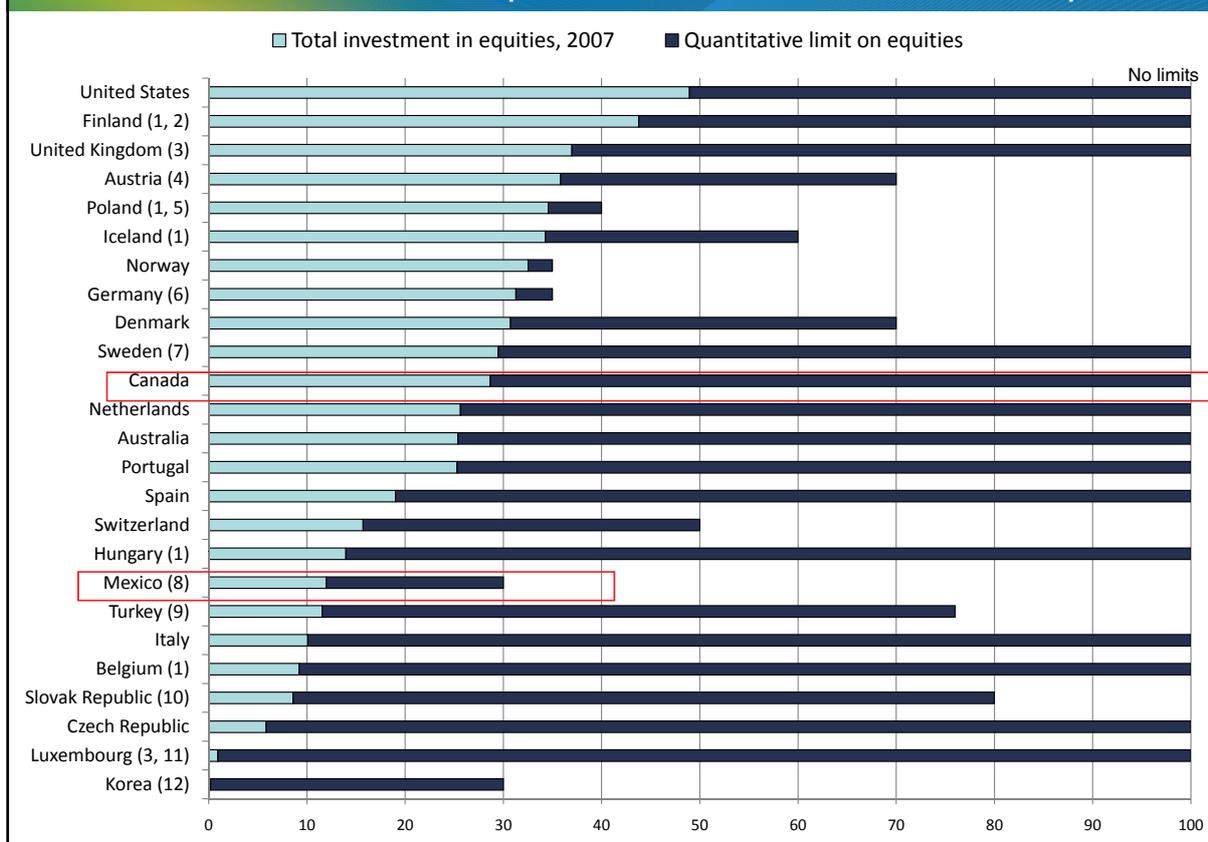


## Changing asset allocation of pension funds

Chart 8: Changes in broad asset allocation for selected countries (2007–2011)



## Portfolio limits on OECD pension funds' investment in equities



## Alternative assets for pension funds

- Of alternative asset classes, real estate is the largest block for pension funds (around 55%), followed by private equity FoF (18%), FoHF (12%), and infrastructure (12%), and commodities (3%). \*
- It has been estimated that less than 1% of pension funds worldwide are invested in infrastructure projects.

\*: Tower Watson, Alternative Investment Survey 2011

## Investment portfolio allocation, life insurers 2010



Notes: Data exclude assets linked to unit-linked products where risk is fully borne by policyholders.

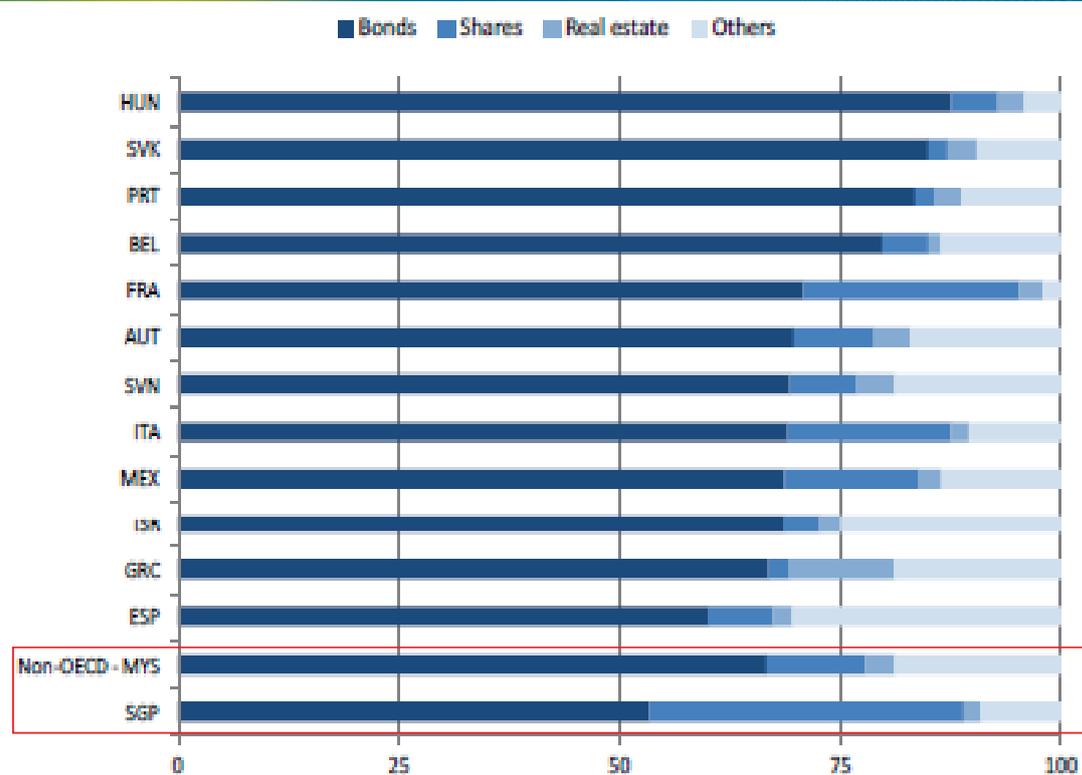
Source: OECD Global Insurance Statistics.

## Investment portfolio allocation, non-life insurers 2010



Source: OECD Global Insurance Statistics.

## Investment portfolio allocation, composite insurers 2010



## Sources that may affect investment behaviour of institutional investors

- Market access measures for foreign investors
- Solvency II or risk-based solvency
  - Related to the above, capital charges towards alternative investments
- Implementation of fair valuation for accounting and regulatory purposes
- Changing provision of products, in particular, moving away for long-term, guaranteed products
- Qualitative/quantitative limits on investment
- Tax incentives

## EXHIBIT 4: CAPITAL REQUIREMENTS FOR SOVEREIGN DEBT

### A. SOLVENCY II

DURATION	AAA	AA	A	BBB	BB	≤ B	NR
1	0.00%	0.00%	0.62%	0.78%	1.40%	2.52%	1.68%
2.5	0.00%	0.00%	1.54%	1.96%	3.50%	6.30%	4.20%
5	0.00%	0.00%	3.08%	3.92%	7.00%	12.60%	8.40%
10	0.00%	0.00%	6.16%	7.84%	14.00%	25.20%	16.80%
25	0.00%	0.00%	15.40%	18.03%	18.20%	25.20%	20.16%

### B. BASEL III

DURATION	AAA	AA	A	BBB	BB	B	CCC	NR
1	0.36%	0.45%	0.86%	2.15%	6.14%	14.16%	25.86%	2.15%
2.5	0.86%	1.02%	1.40%	3.40%	8.15%	16.22%	27.55%	-3.40%
5	1.69%	1.95%	2.93%	5.50%	11.49%	19.65%	30.36%	5.50%
10	1.69%	1.95%	2.93%	5.50%	11.49%	19.65%	30.36%	-5.50%
25	1.69%	1.95%	2.93%	5.50%	11.49%	19.65%	30.36%	5.50%

### C. NAIC – LIFE

DURATION	AAA	AA	A	BBB	BB	B	CCC
Any	0.84%	0.84%	0.84%	2.73%	9.66%	21.00%	48.30%

### D. NAIC – P&C

DURATION	AAA	AA	A	BBB	BB	≤ B	CCC
Any	0.63%	0.63%	0.63%	2.10%	4.20%	9.45%	21.00%

## EXHIBIT 3: CAPITAL REQUIREMENTS FOR CORPORATE BONDS

### A. SOLVENCY II CAPITAL FACTORS

DURATION	AAA	AA	A	BBB	BB	≤ B	NR
1	0.50%	0.62%	0.78%	1.40%	2.52%	4.20%	1.68%
2.5	1.26%	1.54%	1.96%	3.50%	6.30%	10.50%	4.20%
5	2.52%	3.08%	3.92%	7.00%	12.60%	21.00%	8.40%
10	5.04%	6.16%	7.84%	14.00%	25.20%	33.60%	16.80%
25	12.60%	15.40%	18.03%	18.20%	25.20%	33.60%	20.16%

### B. BASEL III CAPITAL FACTORS

DURATION	AAA	AA	A	BBB	BB	B	CCC	NR
1	0.36%	0.63%	1.59%	4.07%	9.06%	16.86%	26.12%	4.07%
2.5	0.86%	1.30%	2.67%	5.78%	11.25%	18.88%	27.79%	5.78%
5	1.69%	2.41%	4.46%	8.63%	14.90%	22.25%	30.57%	8.63%
10	1.69%	2.41%	4.46%	8.63%	14.90%	22.25%	30.57%	8.63%
25	1.69%	2.41%	4.46%	8.63%	14.90%	22.25%	30.57%	8.63%

### C. NAIC – LIFE CAPITAL FACTORS

DURATION	AAA	AA	A	BBB	BB	B	CCC
Any	0.84%	0.84%	0.84%	2.73%	9.66%	21.00%	48.30%

### D. NAIC – P&C CAPITAL FACTORS

DURATION	AAA	AA	A	BBB	BB	≤ B	CCC
Any	0.63%	0.63%	0.63%	2.10%	4.20%	9.45%	21.00%

## Concluding remarks

- Despite the economic downturn, there continues to be a trends towards liberalisation of the financial sector.
- There has been increasing interest from Asian countries to have active institutional investors create a robust investment basis in their markets.
- Given the large potential for insurance and pension funds to grow in Asian market, it seems sensible to provide greater investment opportunities to funds, both domestically and internationally, and possible alternative investment opportunities to retail investors away from saving products.
- Associated prudential and consumer protection measures should be taken to ensure the safety of the financial system.
- Scope for data collection on institutional investors' activities (insurers and pension funds) in emerging markets.