



**Kingdom of Cambodia**  
**Nation Religion King**

**OPENING ADDRESS**  
**BY**  
**HIGHEST REPRESENTATIVE OF THE PRIME MINISTER**  
**OF THE KINGDOM OF CAMBODIA**  
**DEPUTY PRIME MINISTER KEAT CHHON, PM**  
**MINISTER OF ECONOMY AND FINANCE**  
**AT THE OPENING CEREMONY**  
**45<sup>TH</sup> SOUTH EAST ASIA CENTRAL BANKS (SEACEN)**  
**GOVERNOR'S CONFERENCE**  
**SIEM REAP, CAMBODIA**  
*Friday, 26<sup>th</sup> February 2010*

*H.E. Chea Chanto, Governor of the National Bank of Cambodia,*

*H.E. Dr. Zeti Akhtar Aziz, Governor of Bank Negara Malaysia*

*Governors and Heads of Delegations of SEACEN central banks and observer banks,*

*H.E. Greenwood, Vice President of the ADB*

*Mr. Hervé Hannoun, the Deputy General Manager of the BIS,*

*Distinguished speakers and guests,*

*Ladies and Gentlemen,*

1. On behalf of **Samdech Akka Moha Sena Padei Techo HUN SEN, Prime Minister of the the Kingdom of Cambodia** and on my own behalf, I would like to extend my warmest welcome to the Governors of the South East Asia Central Banks (SEACEN) Group to Siem Reap on this occasion of the 45<sup>th</sup> Annual SEACEN Governor's Conference on **"The Role of the Central Bank in Sustaining Economic and Achieving Financial Stability,"** and the 29<sup>th</sup> Meeting of the SEACEN Board of Governors.

2. At the outset, I would like to say I am delighted and honored to be at this auspicious occasion, in the company of distinguished representatives from the ADB, IMF and BIS, who came

all this way to share with us their expertise and knowledge at this important event of the SEACEN family.

### **Policy Response to the Global Financial Crisis**

3. After the Asian Financial Crisis, Asian countries embarked on bank restructuring and structural reforms, which contribute to strong economic growth and financial stability. However, 2009 was a turbulent time for Asia and the world as a whole. Even though Asia's financial institutions have limited direct exposure to the US sub-prime mortgages and East Asian countries have strong external positions, nonetheless Asia was hit by the Global Financial Crisis because of the collapse of international trade and capital flows.
4. At the initial stage of the crisis, all countries in the region experienced capital outflows driven by deleveraging. Liquidity of the banking system tightened and the credit market dried up. The crisis resulted in the collapse of the international trade. This in turn has had negative impact on the real economy, posing considerable risks on the financial system.
5. The central banks responded by easing monetary policy: lowering policy rates. However, conventional monetary easing has had a limited impact on financial conditions and in normalizing credit intermediation, necessitating a number of quantitative measures, fiscal stimulus, and regional cooperation. This has led to a rapid expansion of public balance sheets, including those of central banks. Moreover, with the collapse of oil prices, inflation was no longer the target of monetary policy. It is worth noting that the Chiang Mai Initiative (CMI), the bilateral SWAP arrangement to the amount of US\$77 billion, in conjunction with the regional surveillance mechanism in the form of Economic Review and Policy Dialogue (ERPD), have played an important role in maintaining the stability. In response to the crisis, ASEAN+3 decided to launch the Chiang Mai Initiative Multilateralization (CMIM) and increase the size of the SWAP arrangements to US\$120 billion.
6. As shown in the advanced economies, the sharp corrections in asset prices resulted in wealth destruction, while households and firms face greater difficulty in gaining access to credit, creating a vicious cycle of de-leveraging between the real economy and the financial sector. As a result, private spending by households and firms collapsed. In this regard, the global financial crisis has

returned fiscal policy as a major macroeconomic tool. Fiscal policy is providing important support to the economy through large stimulus package to support domestic demand. While public spending is critical to bolster aggregate demand and to limit the impact of the financial crisis on the real economy, it implies a significant deterioration in the fiscal accounts. Therefore, a large fiscal space and moderate public debt are important to maintain confidence in medium-term fiscal sustainability. We have to draw a lesson from what happens in some countries in Europe.

## Exit Strategy

### *Excellencies, Ladies and Gentlemen!*

7. Although the global recovery remains fragile, we expect growth in Asia excluding Japan in 2010 to be around 7 percent. This means that emerging market economies should be able to exit from crisis support measures sooner than the advanced economies. Asia's remarkable recovery seems to reflect to some extent a decoupling from the United States and Europe. The main factors contributed to Asia's rebound include global trade normalization, especially in the global IT recovery, monetary easing, currency flexibility, sound balance sheets of its private sector and large fiscal stimulus. In this regards, I wish to quote Mr. Dominique Strauss-Kahn, IMF Managing Director, as saying "*Asia is leading the world in terms of economic recovery from the crisis; and over the coming decades, the region's continued dynamism will give it an even greater role*". This message indeed signals an increasing role of the region's central bankers and particularly the importance of today SEACEN meeting.

8. In this regard, timing exit strategy is crucial. Fiscal and monetary stimulus should be maintained until recovery is firmly in place. There is a consensus that the withdrawal of stimulus should await a more clear-cut and sustained recovery in private demand, as well as a return to more entrenched financial stability. Therefore, strong growth must be restored, while structural reform is needed to boost productivity and create new investment. Efforts to boost the "green" economy can also support this restructuring effort. Financial sector reform should be continued to widen the parameter of regulation and further improve supervision. Key medium-term challenge in Asia, however, is to allow domestic sources of growth to play a more dynamic role. International economic cooperation will be strengthened to facilitate stable and balanced growth.

## Cambodia's Policy Response to the Crisis

### *Excellencies, Ladies and Gentlemen!*

9. Let me now share with you some of the initiatives underway in Cambodia as we have struggled to maintain monetary stability and support sustainable economic growth. Cambodia is a small and open economy, with capital account liberalization. Cambodian economy is highly dependent on a sustained international trade expansion and foreign capital inflow. More than 90% of the banking transactions are dollarized. It means that we cannot use interest rate policy to influence the economy. With free capital flow, foreign exchange intervention has been used to stabilize the exchange rate and to increase international reserve position. Policy response coordination, through the Committee for Economic and Financial Policies, is crucial in a dollarized economy, in which fiscal policy also plays a crucial role.

10. During the high oil and food price crisis in 2008, our Committee for Economic and Financial Policies set up a joint taskforce involving the Ministry of Economy and Finance, the National Bank of Cambodia and key economic ministries to enhance economic surveillance efforts and provide more coordinated policy response. Reserve requirement was increased from 8% to 16%, while commercial bank's exposure to high risk sector was capped. After the onset of the Global Financial Crisis, we reduced the reserve requirement to 12%, lifted lending restrictions, and increased spending to boost domestic demand. In addition, the central bank has made further efforts to improve supervision and regulation by tightening rules and regulations and enhancing onsite supervision. Particular attention has been made to the banks' solvency and liquidity conditions. Further regulatory and supervisory measures will be implemented to strengthen risk management and corporate governance at the banks to strengthen enabling institutions to better anticipate, manage and ultimately withstand adverse economic conditions and market trends.

11. On the fiscal front, the Royal Government of Cambodia has acted counter-cyclically to boost domestic demand, with increased public expenditure towards improving social safety nets and providing retraining and alternative employment for vulnerable population segments, including those losing jobs in the affected export sectors. We have also established the Fund for Agricultural Development in order to increase agricultural productivity and diversify our growth base. Priorities

have also been given to public investment in physical infrastructure and supporting growth in the agricultural sector.

### **Lessons for Financial Regulation and Supervision**

12. Ensuring financial stability involves both the preservation of macroeconomic stability and the promotion of a strong and sound institutional framework for the financial sector; weakness in one of these pillars could negatively affect the performance of other. And as we all have witnessed, the recent crisis has tested the effectiveness of various macroeconomic policies in restoring economic and financial stability, while bringing into question the adequacy of the existing regulatory and supervisory framework.

13. The principal mission of the central bank is to promote price stability and a stable financial system. It is recognized that promoting price stability is not an end in itself. By running monetary policy to maintain price stability, central banks can avoid excessive volatility in the purchasing power of the money that they issue, minimize large swings in financial markets and thus provide an environment conducive to sustainable growth in output and employment. However, lessons from the economic and financial crisis thus far have also taught us that a prolonged period of price stability can be a fertile ground for excessive optimism, driving asset prices to unrealistic levels and causing financial distress. The challenge for the central banks is therefore on one hand to provide appropriate financing to the economy while taking into account the very significant balancing of inflationary risks and financial stability.

14. A study prepared by the IMF shows that, I quote: *“Interest rates are a poor tool to deal with excess leverage, excessive risk taking, or apparent deviations of asset prices from fundamentals. We need a combination of monetary and regulatory tools. We should use specific instruments to deal with specific issues: regulatory capital ratios can be increased, if leverage is excessive; liquidity ratios can be increased if liquidity is low; loan-to-value ratios can be decreased to dampen housing prices; margin requirements can be raised to limit stock price increase”*. These specific instruments can have a more targeted impact than the policy rate. It’s better to use the policy rate primarily in response to aggregate activity and inflation.”

15. The crisis has led to a re-assessment of our growth models and the role of capital flows. Building a strong post-crisis world would require balanced growth. Economic policies, therefore, must be consistent with healthy external positions. This means maintaining sound fiscal, monetary, and exchange rate policies, and also avoiding domestic market distortions. For this economic transformation to be successful, international policy collaboration will need to be more effective. We must identify the key elements of a new model that can deliver sustained economic growth. In particular, we realize that because there are limits to the pace of export growth, domestic and regional demand will need to play an increasingly important role in underpinning Asia's growth. As saving rates in advanced economies are expected to rise, Asia is required to develop a sound bond market to absorb the accumulation of reserves, which play a crucial role in confidence building during the crisis. This means reinvigorating domestic demand and boosting intraregional trade. We must step up our efforts to increase public investment in infrastructure and education. In this regard, I would like to commend the efforts made by the ADB in developing the Asian Bond Market and assisting the efforts of the ASEAN Finance Ministers to establish the ASEAN Infrastructure Fund (AIF).

16. We have seen that capital flows can play a crucial role in sustaining economic growth, but also can undermine financial stability. Although capital inflows are much welcomed, policymakers are concerned now with how to manage these flows—their impact on exchange rates, domestic demand, financial stability—and the potential danger of asset bubbles. There are different coping mechanisms, including allowing exchange rate to adjust, lowering interest rates, accumulating reserves, tightening fiscal policy, macro-prudential policies in the financial sector, as well as temporary capital controls. I hope that these issues will be discussed at the conference.

17. Another regulatory issue is to discourage banks from taking excessive risks and to use liquidity to stimulate investment and job creation. Stiglitz said that if financial institutions had allocated the abundant liquidity to jobs and investment, the world economy would be in much better shape now. He added that "When they win they walk off with the profits, when they lose the taxpayer pays," he pointed out. "We really need to go more directly at these issues like incentives."

18. I would like to conclude by emphasizing that the current crisis has required the central banks to assume more roles in promoting both economic and financial stability. However, this is a very complex matter because the linkage between the two goals goes in both directions and can take many forms. My view is that, though central banks have an important role in attaining these twin goals, other public authorities such as the Ministry of Economy and Finance and other bodies in charge of supervising particular financial institutions should also shoulder part of the responsibility. Given the interdependence of the financial markets, and the contagion effects of risks emanating from one sector to another, there is a need to strengthen coordination between relevant authorities.

19. Now is the time for us in Asia to use its stronger voice to contribute even more to the shaping of the post-crisis global economic landscape. Regional cooperation is also critical in addressing macroeconomic imbalances and financial risks arising from events outside individual country border. I therefore wish to congratulate the concerted efforts of the SEACEN member banks in discussing how central banks should respond to these new challenges and changes. On this note, I wish you all great success in your endeavors.

20. Finally, may I now officially declare the opening of the 45<sup>th</sup> Conference of the SEACEN Governors and 29<sup>th</sup> Meeting of the SEACEN Board of Governors.

Thank you!

