

# Recovery on Track ?

## Lessons from the Asian Economic Crisis

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### Introduction

Some years ago, people started talking about a possible slowdown of the economic development among the Asian countries and ASEAN in particular. However, it was not only until the summer of 1997 that the Asian economic crisis erupted with the collapse of currencies and stock markets in Southeast Asia. On 2 July, a drastic drop in the Thai currency and stock market indicated the beginning of the Asian economic crisis. Until recently, most of the Asian countries (Indonesia, Korea, Thailand and Malaysia in particular) were in one way or the other, suffering from economic depression, political chaos and social instability. Indonesian President Suharto was forced to resign on 2 May 1998, indicating that the chaotic situation in Southeast Asia had reached its most serious level. However, in late 1998 some signs of improvement could be observed.

In Japan, Hashimoto Ryutaro resigned after a crushing defeat in Upper House elections in July 1998. Hashimoto was the fourth leader (following Gen. Chavalit Yongchaiyudh in Thailand, Kim Young Sam in Korea and Suharto in Indonesia) to resign in Asia within a year after the eruption of the Asian economic crisis. Obuchi Keizo had been elected (24 July 1998) president of the Liberal Democratic Party and subsequently became the Prime Minister of Japan. Very few observers within and outside Japan expected him to efficiently rectify the Japanese economy and put it on the right track within a year. If the sluggish economic situation in Japan were to drag on it would definitely delay the recovery of the Asian economies much beyond our expectations.

In the meantime, China's economic development is the main concern, particularly within the Asia-Pacific region. Can China successfully restructure its state-owned enterprises within three years, as promised by the Chinese Premier Zhu Rong Ji ? Can China succeed in attaining 8 per cent GDP growth without depreciating the Renminbi ? (China maintained approximately 8.3

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Reminbi to the dollar over the period 1994-1998) . Chinese leaders have on many occasions, particularly during the period March-July 1998, announced that China would not depreciate its currency so as to avoid further aggravation of the economic crisis in Asia. However, if the Japanese Yen resumes depreciating (say around 150 to the US dollar) or if the Asian economies, like Indonesia, Korea and Thailand further deteriorates, China will depreciate her currency (as she did in 1994 by depreciating the Renminbi by more than 33 per cent) . This is simply because China has already felt the impact since January 1998 and cannot afford to substantially reduce her exports or direct foreign investments, as she intends to keep a high GDP growth.

All in all, Asian countries are suffering from serious economic difficulties. At this moment, do we perceive the Asian currency crisis and a slump in stocks in Asia as a fundamental economic crisis, or simply due to Southeast Asian economies having just entered into a transitional period of economic restructuring ? In other words, do we perceive the currency crisis and a slump in stocks in Asia as a common syndrome and a defect in the economic structure among the Asian countries, or simply a temporary economic confusion due to the mismanagement of macroeconomic (both monetary and fiscal) policies ?

This article is aimed at analysing the substance of the Asian currency crisis and to predict the recovery prospects of the Asian economies. The Asian currency crisis is perceived here as an economic crisis accompanied by a serious economic downturn and basically due to the failure of macroeconomic policies implemented by the Asian countries. However, it is believed that this economic crisis can be overcome and the Asian economic recovery can be put back on the right track (say within 2 years) , should resolute and timely macroeconomic rectification policies be implemented.

The Asian currency crisis erupted in Thailand and spread to the ASEAN countries and then to the NIEs. The so-called Blue Monday occurred on 27 October 1997, caused by the drastic drop in currency and stocks in Hong Kong, which in turn forced stocks in USA and Japan to drop almost simultaneously. The Blue Monday was just 10 years after the Black Monday that occurred on 19 October 1987. Stocks in the USA dropped by 554.26 points on Blue Monday compared to 508.00 points on Black Monday. A slump in stocks in the USA caused chaotic stock markets in Europe, South America, Mexico and then throughout the World.

Fortunately, between the 29-31 October, stocks in the USA and Japan rebounded, and the Blue

Monday crisis was resolved, at least temporarily. Likewise, the Asian currency and economic crisis can never be treated in isolation. A new shock, triggered by a financial crisis in Russia, was delivered in the summer of 1998. After that, the stock markets of Asia started recovering. the “real” side of the economy is still hurting, however. Should the Japanese economy drag on with no sign of rapid recovery since the bubble economy collapsed in March 1991, the Asian economies in general and the Chinese economy in particular, will no doubt be adversely affected. The sluggish economies in Asia will further adversely affect the economies in Europe and the USA.

### **1. Current Balance Deficit-A Failure of Monetary and Fiscal Policies**

Current balance consists of the following items:

- Trade balance (balance of export and import trade)
- Balance of invisible trade (transportation, insurance, travel, investment earnings etc.)
- Balance of transfer (services and the sum of cash transactions etc.)

Here we are only discussing the trade balance, as it is the most important part of the current balance.

As can be seen from Tables 1 and 2, the ASEAN countries have been suffering seriously from current balance deficits in recent years. In 1996, Thailand, Indonesia and Malaysia suffered from current balance deficits amounting to US\$14.4 billion (8.1 per cent in terms of GDP) , US\$7.8 billion (3.4 per cent) and US\$4.8 billion (4.9 per cent) respectively. It can therefore be suggested that one of the detrimental factors that contributed to the collapse of the currencies and stocks in ASEAN was the weak monetary and fiscal condition of these countries.

Among the NIEs, over the period 1993-1997, Singapore and Taiwan recorded a substantial amount of current balance surpluses. In 1997, Singapore and Taiwan benefited from US\$14.8 billion (15.6 per cent in terms of GDP) and US\$7.7 billion (2.7 per cent) current balance surpluses respectively. Hong Kong's current balance surpluses decreased substantially from US\$9.9 billion in 1993 to merely US\$3.1 billion in 1994. In 1995, Hong Kong suffered a current balance deficit that amounted to US\$3.4 billion. As for Korea, it suffered current balance deficits during the period 1994-1997. In 1996 in particular, Korea's current balance deficit amounted to US\$23.0 billion (4.4 per cent in terms of GDP) .

The above mentioned figures have somehow explained why the Asian economic crisis only marginally affected the economies in Singapore and Taiwan. However, with tremendous current balance deficits, Hong Kong and Korea are suffering from continuous economic downturn,

political instability and social chaos. In 1998, Hong Kong and Korea suffered from  $-5.1$  per cent and  $-5.8$  per cent GDP growth.

It is therefore clear that the recent currency crisis and stock market collapse struck first in those economies with sizeable current balance deficits. The large current balance deficits have become a great pressure on the overvalued currencies in Asia and have functioned as a determining factor in the depreciation of currencies and the collapse of the stock markets in Asia.

Table 1 Current Balance of the Asian Countries

(Unit : million US dollars)

		1993	1994	1995	1996	1997	1998
ASEAN							
	Indonesia	-2,106	-2,792	-7,023	-7,801	-5,824	—
	Malaysia	-3,079	-5,628	-8,644	-4,847	-5,031	9,199
	Philippines	-3,016	-2,950	-1,893	-3,953	-4,351	1,294
	Thailand	-6,364	-8,085	-13,554	-14,691	-3,024	14,290
NIEs							
	Korea	990	-3,867	-8,508	-23,005	-8,167	40,039
	Taiwan	7,042	6,489	5,474	11,027	7,688	3,728
	Hong Kong	9,872	3,135	-3,401	-2,133	-5,184	—
	Singapore	4,272	11,453	14,361	14,723	14,803	17,524
	USA	-90,771	-133,538	-129,095	-148,184	-166,446	
	China	-11,902	7,657	1,620	7,242	29,717	—
	Japan	131,915	130,540	110,421	65,802	94,523	121,167

Source : Compiled from Keizai Kikaku-cho, Ajia Keizai (Asian Economics), various issues

Table 2 Current Balance of the Asian Countries In Terms of GDP

(Unit : %)

		1993	1994	1995	1996	1997	1998
ASEAN							
	Indonesia	-1.3	-1.6	-3.5	-3.4	-2.7	—
	Malaysia	-4.8	-7.8	-10.0	-4.9	-5.1	13.0
	Philippines	-5.5	-4.6	-2.7	-4.8	-5.3	2.0
	Thailand	-5.1	-5.6	-8.1	-8.1	-2.0	12.3
NIEs							
	Korea	0.3	-1.0	-1.7	-4.4	-1.7	12.5
	Taiwan	3.2	2.7	2.1	4.0	2.7	1.4
	Hong Kong	8.5	2.4	-2.4	-1.4	-3.0	—
	Singapore	8.9	15.9	17.0	16.1	15.6	20.7
	China	-2.0	1.4	0.2	0.9	3.3	—
	Japan	3.1	2.8	2.1	1.4	2.3	3.2

Source : Same as Table 1

## 2. International Trade Deficit-A Fatal Result of Rapid Industrialization

Particularly since the second half of the 1980s, Southeast Asian countries had enthusiastically been implementing industrialization policies in order to speed up the economic development process. The implementation of industrialization policies implied that Southeast Asian countries needed to import substantial amount of capital goods, intermediate goods and durable consumption goods from the industrialized nations, especially from Japan, Europe and the USA. International trade relationships between Southeast Asian countries and the industrialized nations have been shifting from vertical to horizontal. However, apparently Southeast Asian countries require a long period of time to break away from the vertical trade structure.

It is particularly essential for Southeast Asian countries to promote horizontal trade relationships with the West in order to correct trade deficits. Especially for resource rich countries such as Indonesia and Malaysia, when prices of primary products are stable or increasing, it would definitely contribute favorably to the international trade of these countries. However, as in the first half of the 1980s, countries producing natural resources suffered a serious blow when prices of petroleum and natural gas dropped drastically. As a matter of fact, most of the Southeast Asian countries have been suffering from substantial trade deficits even when prices of primary products remained stable. Generally, ASEAN and NIEs' trade deficits against Japan have been balanced by trade surpluses with the USA. However, as seen in Table 3, most of the Southeast Asian countries have been suffering from international trade deficits.

Table 3 Trade Balance of the Asian Countries

(Unit : million US dollars)

		1993	1994	1995	1996	1997	1998
ASEAN							
	Indonesia	8,495	8,069	4,789	6,886	11,763	21,745
	Malaysia	1,489	-762	-3,737	-101	-16	14,893
	Philippines	-6,268	-7,808	-9,168	-11,884	-10,706	-159
	Thailand	-9,147	-9,329	-14,317	-16,602	-3,749	11,446
NIEs							
	Korea	-1,564	-6335	-10,062	-20,624	-8,452	39,031
	Taiwan	8,030	7,700	8,109	13,572	7,656	5,917
	Hong Kong	-3,410	-10,437	-19,001	-17,800	-20,555	-10,583
	Singapore	-11,219	-5,938	-6,207	-6,320	-7,404	8,302
	China	-12,215	5,391	16,696	12,230	40,420	43,600
	Japan	120,241	120,858	106,843	61,941	82,501	106,886

Source : Same as Table 1

Over the period 1993-1997, resource rich Indonesia was the only country in ASEAN to benefit from a trade surplus. Malaysia, the Philippines and Thailand were trade deficit countries. Trade deficits in Thailand and the Philippines were particularly serious. In 1996, trade deficits in these two countries amounted to US\$16.6 billion and US\$11.8 billion respectively (see Table 3)

Among the NIEs, Taiwan was the only trade surplus country over the period 1993-1997. The re-export trade factor should be taken into consideration, as Hong Kong and Singapore are entrepot economies. Besides, as mentioned earlier, Hong Kong and Singapore had recorded current balance surpluses as they had healthy invisible trade balances.

Korea's trade deficit increased substantially year by year over the period 1993-1997. In 1996, it amounted to US\$20.6 billion.

Judging from the above mentioned figures, it is not surprising to notice that the recent Asian currency crisis and the collapse of the stock markets occurred in countries with substantial trade deficits (weak financial base) (i.e. Thailand and Malaysia among the ASEAN countries and Korea among the NIEs) .

### **3. Accumulation of Foreign Debts-A Heavy Burden of Economic Development**

It has been a common feature that the Asian countries financed their domestic industries, social and industrial infrastructure and big industrial projects by borrowing heavily from the highly industrialized countries and international financial institutions (for example the International Monetary Fund, the World Bank and the Asian Development Bank) . Presently, there are many countries in Asia whose foreign debts have accumulated substantially in recent years so that they are unable to pay back the debts.

Japan has since 1989 wrested from the West the title of the world's largest official development assistance (ODA) nation. Japan's ODA increased remarkably from US\$8.9 billion in 1989 to US \$14.7 billion in 1995. In 1970,98.2 per cent of Japan's ODA was concentrated in Asia. However, in 1995 the degree of concentration dropped to 54.4 per cent. In recent years, China, Indonesia, India, the Philippines and Thailand have been Japan's largest recipient countries among the Asian countries.

Financial loans from overseas have always been accompanied by foreign exchange risks. The strong and appreciated Japanese currency during the period 1985-1995 has forced the Asian

countries to adopt a policy of postponing the repayment of loans or refinancing. In April 1995, the yen debtor countries in Asia fell into a chaotic situation, as the yen soared to 78 to the dollar. Loan repayment by Asia to Japan became impossible. Although the yen depreciated thereafter, the Asian currencies have suffered an even greater drop at the same time. To make it worse, the yen is rising again nowadays.

The fall of the Asian currencies and the accumulation of foreign debts are somehow interrelated. Table 4 reveals that the Asian countries, particularly Indonesia, China and Thailand, have suffered from excessive foreign debts. In 1996, foreign debts of these three countries amounted to US\$129.0 billion, US\$128.8 billion and US\$90.8 billion respectively. Even in 1995, according to Nihon Keizai Shimbun editorial, Indonesia's foreign debt amounted to US\$110.0 billion and was the highest among the Southeast Asian countries. It was reported that government loans and private loans had amounted to US\$50.0 billion and US\$60.0 billion respectively, and if the unreported portion were to be included, the latter should increase to US\$80.0 billion.

Table 4 External Debt Balance of Asian Countries  
(Gross, Hundred million US dollars)

	1992	(D/SR)*	1993	(D/SR)	1994	(D/SR)	1995	(D/SR)	1996	(D/SR)
Indonesia	880	32.6	891	33.6	1,078	30.7	1,244	30.9	1,290	36.8
Philippines	330	24.4	359	25.6	400	18.9	394	16.4	412	13.7
Malaysia	200	9.2	261	8.6	295	9.3	344	7.0	398	8.2
Thai	418	13.8	427	13.7	481	13.5	832	11.6	908	11.5
Vietnam	239	12.7	249	13.2	256	7.3	258	5.0	268	3.5
China	724	10.2	859	11.1	1,005	8.9	1,181	9.9	1,288	8.7

\* D/SR means debt service ratio. D/SR indicated the degree of external debt owed by an individual country. It shows the ratio of external debt repayment compared to the total amount of exports of an individual country. The burden of external debt is high if the ratio is high.

Source : Same as Table 1

Among the NIEs' foreign debts, data on Taiwan, Hong Kong and Singapore are not available. Probably foreign debts of these countries are satisfactory. However, as far as Korea is concerned, its foreign debt amounted to US\$47.2 billion in 1993. As an OECD country next only to Japan in Asia, Korea's case is astonishing.

As for China, her foreign debts particularly have attracted much attention. China's foreign debts have been substantial and comparable to Indonesia over the 1992-1996 period (See Table 4) . By

June 1997, China's foreign debts amounted to US\$118.6 billion and had exceeded Indonesia's US\$ 110 billion. China has become the largest debtor country in Asia. Undoubtedly, the substantial amount of foreign debt has become a dragon in China's economic development. In the meantime, fortunately, the foreign debt issue has not become a serious obstructive or destructive factor in China's economic development, as her other economic fundamentals (in terms of current balance surplus and foreign currency reserves) are in good order. China is now facing some other serious problems, however. The problems include a task to restructure state-owned enterprises, a drastic decrease in export trade (20 per cent decrease in the first half of 1998), an abrupt decrease in foreign direct investments in China (dropping from US\$64 billion in 1997 to probably US\$40 billion-US\$50 billion in 1998) and an immense increase in unemployment. (The unemployed increased from 10 million in 1997 to 16 million in 1998 due to mismanagement of the state-owned enterprises) The most serious problem faced by China at the moment is a drastic increase in bad loans. Presently, the total amount of China's domestic bad loans is as high as 37 per cent of the GDP, compared to 20 per cent of Thailand's.

The accumulation of foreign debts among the ASEAN countries, Korea and China implies weaknesses of the economic constitution and economic fundamentals of these countries. Foreign investors may lose confidence and foreign direct investments could diminish drastically in these countries. All these factors actually, in one way or the other, prompted the collapse of currencies and stock markets in Asia.

#### **4. International Turbulence-Three Big Undercurrents of the Economic Crisis**

The Asian economic crisis burst out initially from the collapse of currencies and stock markets in ASEAN and some NIEs. This economic disturbance was basically due to macro mismanagement-current balance deficit, international trade deficit and accumulation of foreign debts. However, it cannot be ignored that international turbulence also contributed adversely to the outbreak, expansion and intensity of the Asian economic crisis. For convenience, all this international turbulence can here be termed as Chinese turbulence, Japanese turbulence and American turbulence.

##### **• The Chinese turbulence**

21 years have passed since China implemented open door and reform economic policies in 1978. The Chinese style socialist market economy has been carried out with an unprecedented impetus. China's economic relationship with ASEAN and NIEs has been complementary as well as competitive. China's relationship with ASEAN and NIEs in the fields of international trade,



foreign investment, technology transfer and economic cooperation have no doubt had many complementary aspects. However, the following competitive aspects cannot be ignored. Firstly, the competitiveness of ASEAN and NIEs in international markets has been lowered, as wages and raw materials in China are much cheaper than that in ASEAN and NIEs. Especially in recent years, the Chinese government has depreciated the Renminbi by 33 per cent against the dollar. Chinese industrial products (labor intensive light industrial products and consumer goods in particular) have therefore speedily overwhelmed international markets. Since 1993, China's trade surplus with the USA increased remarkably. In 1996, China's trade surplus (inclusive of Hong Kong's exports to the USA) with the USA amounted to US\$40 billion. The abrupt increase in China's exports to the USA implied sudden decrease of ASEAN and NIEs exports to the USA. In other words, exports of ASEAN and NIEs industrial products within the same category as China's have been restricted. Secondly, European, American and Japanese direct foreign investments in China increased substantially while those in ASEAN and NIEs decreased abruptly. Foreign capital to be invested in ASEAN and NIEs have been redirected to China. Ironically, investments from ASEAN and NIEs have also been lured to China. A large proportion of their labor intensive industries, with less comparative advantages, are also shifting to China. China has not only become an important recipient country of the foreign direct investments of Europe, the USA and Japan, but has also become a large recipient country of ASEAN and NIEs investments. Viewed from this aspect, China is apparently the opponent of ASEAN and NIEs at least in the short term. As a result of sufficient foreign capital in China, ASEAN and NIEs presently suffer from lack of foreign capital in their domestic markets.

### ●The Japanese Turbulence

In December 1971, Japan shifted from the peg system (US\$1 = ¥360) to the floating rate system. Since then, the Japanese currency has fluctuated according to the realities of the Japanese economy. The Japanese currency reached a turning point when the G5 meeting was held in autumn 1985. Just before the G5 meeting, the Japanese exchange market transacted ¥242 to the dollar. The USA currency depreciated drastically and in June 1994, ¥100 was transacted to the dollar. The yen continued to appreciate and in April 1995, the Japanese Yen reached its peak and US\$1 was transacted to ¥78. After the second half of the 1980s, due to the strong yen, Japanese direct foreign investments in Asia increased remarkably. Until the collapse of the Japanese bubble economy in March 1991, Japan, both from supply and demand sides, contributed tremendously to the economic development of the Asian countries.

Through the January 1991-April 1995 period, the Japanese currency maintained its strength. Over the above-mentioned period, both Japanese direct investments in Asia and the reverse export from Asia to Japan should have been strengthened. However, Japanese domestic markets were extremely sluggish due to the collapse of the bubble economy. Exports from Asia to Japan had not been satisfactorily stimulated as deregulation and the opening up of Japanese domestic markets had not fully materialized.

The Japanese currency started to depreciate soon after it reached its peak in April 1995. Over the April 1995-October 1997 period, Japanese exports were largely stimulated due to the drastic depreciation of the yen. Japan's trade surplus, especially against the USA, increased abruptly. In parallel with the immense increase of Japan's international trade, Asian export trade stagnated.

Actually, in 1995, ASEAN's exports were promising. Exports of machinery from ASEAN (especially Malaysia and Thailand) to Japan increased substantially to such a high level that it constituted one third of Japan's total machinery imports in the same year. Exports of machinery from ASEAN to the USA and NIEs had also increased remarkably. However, in 1996, the growth rate of exports from Asia including ASEAN decreased abruptly. Total growth rate of exports from NIEs dropped from 21.0 per cent in 1995 to merely 4.3 per cent in 1996. Both growth rates of exports from ASEAN (Indonesia, the Philippines, Malaysia and Thailand) and China dropped drastically from 22.7 per cent to 5.1 per cent, and from 22.9 per cent to 1.5 per cent, respectively.

In 1996, the growth rates of exports from Asia to Japan had also shown a similar tendency. For Singapore, it decreased from plus 47.3 per cent to plus 5.7 per cent. For Thailand and Malaysia, it decreased from plus 23.8 per cent to plus 0.8 per cent, and from plus 28.2 per cent to plus 11.4 per cent respectively. Even for China, it decreased from plus 30.3 per cent to plus 12.6 per cent. Furthermore, if we confine it to machinery exports from Asia to Japan, Korea's exports growth dropped from plus 57.8 per cent in 1995 to minus 13.2 per cent in 1996, Thailand's exports growth decreased from plus 51.5 per cent to plus 10.5 per cent and Malaysia's decreased from plus 53.1 per cent to plus 22.2 per cent.

From the above analysis, it is clear that Japan's exports had been stimulated after the yen depreciation from 1995 onwards. However, due to the sluggish domestic markets in Japan, ASEAN and NIE's growth rate of exports to Japan dropped substantially. Obviously, a drastic

slowdown in the export trade of ASEAN and NIEs to Japan had in general worsened further both the current balance and trade balance of the Asian countries. Japanese turbulence in this sense no doubt contributed adversely to the present Asian economic crisis.

### ●The American Turbulence

Since the second half of the 1980's, ASEAN and NIEs have succeeded in rapid economic development. One of the most important contributing factors, as mentioned earlier, was Japan's heavy investment in Asia. The other essential factor for the Asian success was undoubtedly due, as an enormous absorber of Asian manufacturing products, to gigantic domestic markets provided by the USA.

The Reagan regime was formed in 1981. Reaganomics produced a substantial amount of "Twin Deficits" (fiscal and trade) on the one hand, and stimulated a great flow of manufacturing products from Asia and Japan in particular on the other hand. The USA eventually started "bashing Japan", started through the G5 meeting in autumn 1985, when the USA was no longer able to bear the burden of the "Twin Deficits". Almost at the same time, the USA started "bashing NIEs" by forcing the currencies of the NIEs (except Hong Kong, as its currency has been pegged to the dollar) to appreciate. Exports from Japan and NIEs to the USA were then efficiently restricted. The sustainable Asian economic development was then seriously affected.

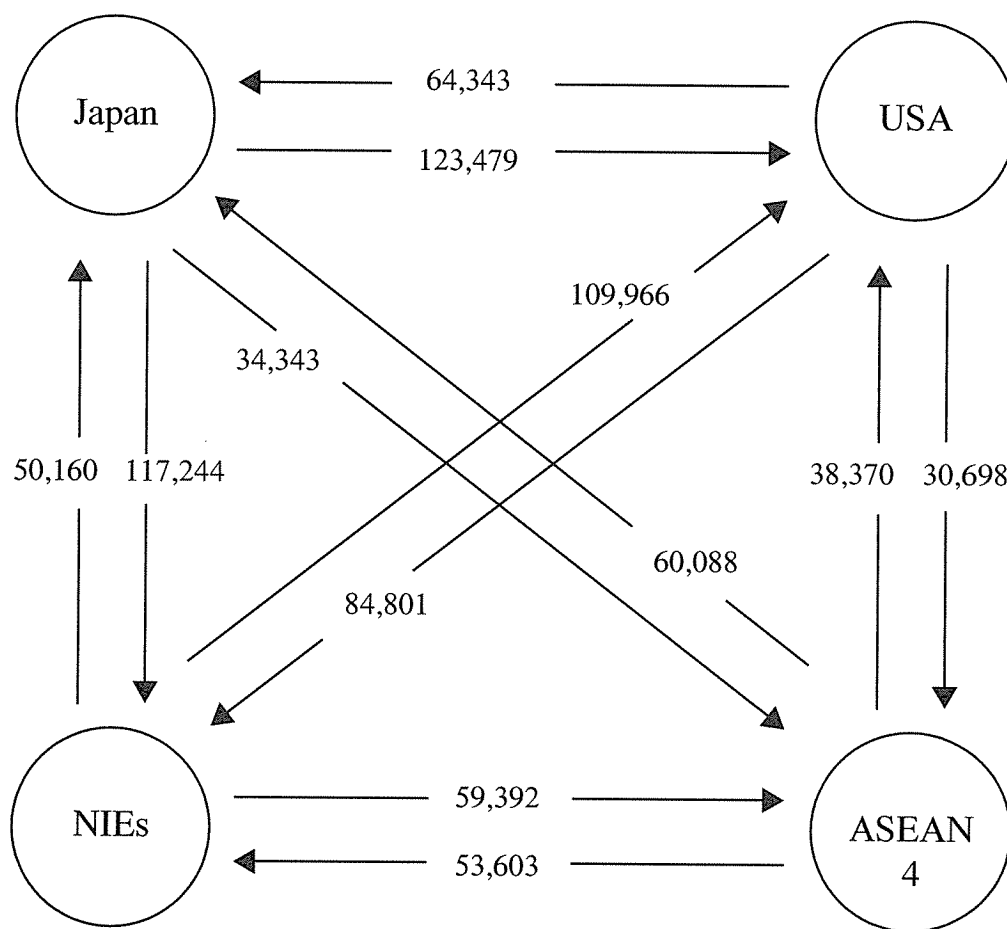
In January 1988, the Reagan regime further announced that the Generalized System of Preferences (GSP) enjoyed by NIEs should be removed from January 1989. This announcement shocked the NIEs. Exports from NIEs to the USA have been seriously affected since the removal of the GSP in January 1989. The international trade mechanism of NIEs, trade deficits with Japan being financed by trade surpluses with the USA, was totally disrupted.

ASEAN's international trade mechanism has been similar to that of the NIEs. ASEAN's exports to the USA had been stagnating when it met with the Chinese and Japanese turbulence. ASEAN's trade deficits were aggravated, as ASEAN's trade deficits with Japan could not be covered by trade surpluses with the USA. As mentioned earlier, stimulated by the yen depreciation, Japan's exports increased substantially after April 1995. In the same year, despite the fact that exports from ASEAN and NIEs to Japan increased substantially, ASEAN and NIEs suffered from serious trade deficits with Japan. Table 5 reveals that in 1995, both ASEAN (Indonesia, the Philippines, Malaysia and Thailand) and NIEs recorded US\$25.7

billion and US\$67.0 billion of trade deficits with Japan, respectively. These trade deficits could hardly be counterbalanced by ASEAN and NIEs' trade surpluses with the USA (US\$7.6 billion and US\$25.1 billion respectively) . ASEAN and NIEs trade deficits amounted to US \$ 60 billion. ASEAN and NIEs current balance and trade balance deteriorated due to the diminishing exports from ASEAN and NIEs to Japan and the USA.

Table 5 Supplementary Relationship in the Asia – Pacific Region(1995)

Unit: million US dollars



NIEs ( 25,165 ) -USA	ASEAN 4 ( 7,672 ) -USA
NIEs ( -67,084 ) -Japan	ASEAN 4 ( -25,745 ) -Japan
NIEs ( 5,789 ) -ASEAN 4	Janan ( 59,137 ) -USA

Source: Same as Table 1

## **5. Disturbing Factors of International Speculators-Thirty Percent Responsibility**

It is not easy to prove that international speculators or investors have thrown currencies and stock markets in Asia into confusion. It is also unfair to suggest that international speculators were the main culprits of the Asian economic crisis. However, if someone suggests that the present economic chaotic situation had nothing to do with international speculators, he would be ignorant of Asia.

It was the Malaysian Prime Minister Dr. Mahathir Mohamad, who for the first time criticized an international speculator by mentioning his name. Soon after the Thai currency depreciated on 2 July 1997, Dr. Mahathir repeatedly and angrily criticized Mr. George Soros. His fierce criticisms against international speculators shocked the world.

Malaysian currency and stock markets reacted unfavourably whenever Dr. Mahathir criticized Mr. Soros. The then Malaysian Deputy Prime Minister and Finance Minister, Mr. Anwar Ibrahim had to make statements to clarify the situation. Malaysian opposition party Democratic Action Party had asked the Premier to “make statements with caution”. However, Dr. Mahathir did not stop and instead increased his criticisms of international speculators.

The spokesman of the USA Department of State, Mr. Barnes totally denied that international speculators had plotted the Asian currency crisis, as implied by Dr. Mahathir. He backed Mr. Soros by saying that, “Mr. Soros is a brave man.” He further suggested that “I don’t think that Mr. Soros” activities are conspiratorial. Only economic forces are at work. The market price can only be rectified by healthy economic policies.” He added “we respect Mr. Soros. He has done a lot of good deeds all over the world.” It was very significant that Mr. Barnes made such statements in Malaysia when he accompanied the Minister of State, Mrs. Albright, on a tour of the country on 26 July 1997.

It is reported that Soros (with estimated assets amounting to US\$20 billion) speculated British against the currency during the European currency crisis and made US\$1 billion profits in 1992. However, he allegedly suffered more than US\$2 billion losses in currency speculation in the midst of the recent Asian economic crisis.

Perhaps having this information in mind, the Emeritus Professor of Yale University, J. Tobin, when questioned about “in Asia people criticize international speculators”, replied impatiently, “the judgement of speculators cannot be always correct as they are also human beings.” In addition

the international MIT economist, Professor Paul Krugman, had also criticized Dr. Mahathir. He argued that “I am very surprised as to why the Premier should comment so much.” He further warned that, “it takes two to three years for investors to regain their confidence and succeed in smooth economic development, should policy makers of the Asian countries review the present currency crisis humbly and tackle the problems with pragmatism. However, a complete Asian economic recovery would take a much longer time, should they hysterically look for scapegoats such as Soros.”

The mass media in the West have been overwhelmingly supportive of international speculators. However, in Asia criticisms against speculative activities involving international speculators are conspicuous. The following comments are some examples:

The Chinese former Premier Li Peng commented that “We should consider both the internal factors (the weaknesses of economic fundamentals) and external factors (disruptive activities carried out by international speculators) of Southeast Asian countries”, when he toured Malaysia and Singapore and currency and stock markets collapsed in Thailand.

The Bank of Thailand criticized Soros by name. The Bank commented that “Soros speculated US\$2 billion in currency. He also intends to use US\$6 billion to attack the Thai currency.”

A Hong Kong finance source argued that “On 15 August 1997, Soros’ hedge fund has plotted to sell Hong Kong dollars in the Hong Kong foreign exchange market. The Hong Kong dollar exchange rate dropped instantly, the Hong Kong central bank intervened and purchased a large quantity of Hong Kong dollars.” In addition, Chinese bank representatives attributed Blue Monday (27 October) to the collapse of the Hong Kong currency and stock markets, and argued that “the hedge fund related to Soros had sold Chinese Hong Kong shares (red chips) in the Hong Kong market.”

The former President of Indonesia, Suharto, argued in his annual parliamentary speech (16 August 1997) that speculative transactions by a specific speculator (referring to Soros implicitly) had “worsened the situation of the collapse of the recent Southeast Asian currency and stock markets.”

Comments on international speculators in Singapore have been rather cautious. Singapore Premier Mr. Goh Chok Tong avoided attributing the disruptive factors affecting the

Southeast Asian currency crisis to international speculators. He emphasized the importance of economic fundamentals and the rational management of monetary and fiscal policies. However, the Finance Minister Dr. Richard Hu affirmed that "Singapore will beat back the international speculators should they come to disrupt the exchange market in Singapore." Deputy Prime Minister Mr. Lee Hsien Loong observed that "international speculators do not attack Singapore currency as Singapore fundamentals are sound." It is clear that the Singapore government is also taking the disruptive factors against the Asian currencies by international speculators into consideration.

International hedge funds have always speculated in countries with weak economic fundamentals (current balance deficits, trade deficits, accumulation of foreign debts and low foreign currency reserves) . This explains why international hedge funds have so far not at a large scale attacked Japan, China, Hong Kong and Singapore, as these countries have impressive records of current balance surpluses. Besides, as can be seen from Table6, the above-mentioned countries have, at least, over the 1993-1997 period, accumulated a substantial amount of foreign currency reserves. These substantial reserves can be mobilized to protect and stabilize local currencies whenever they are ill manipulations of international speculators. International speculators have so far aimed at Thailand, Indonesia and Korea and have played a role in further disclosing countries with weak economic fundamentals. It is therefore clear that the present Asian economic crisis is not unrelated to speculative activities led by international speculators headed by Soros. It may be argued that the present Asian economic crisis is due 70 per cent to the weaknesses of economic fundamentals of specific countries, whereas 30 per cent is due to disruptive activities in foreign exchange markets by international speculators.

#### **6. Recent Economic Development in Asia — Is Asia's Recovery Sustainable ?**

For about two months before Lee Teng Hui made his sudden 'state - to - state' announcement on 9 July 1999, most of the countries in the Asia Pacific region had started experiencing some kind of economic recovery. With relatively stable currency exchange rates installed, stock and property markets improving, foreign currency reserves increasing and confidence towards the market economy restored, the Asian economies are on their way to recovery, almost 2 years after the Asian financial crisis erupted on 2 July 1997.

To take a retrospective glance, Asian countries using various policies to tackle the financial crisis can be divided into 3 groups. The first group is basically based on the IMF prescription: deflationary fiscal policies, higher interest rates and thorough industrial restructuring, such as Korea and Thailand. The second group is against the IMF prescription: inflationary fiscal

Table 6 Foreign Currency Reserves of the Asian Countries  
(Unit : million US dollars)

		1993	1994	1995	1996	1997
ASEAN						
	Indonesia	10,988	11,820	13,306	17,820	16,088
	Malaysia	27,249	25,423	23,774	27,009	26,100*
	Philippines	4,546	5,866	6,235	9,902	7,147
	Thailand	24,473	29,332	35,982	37,731	26,179
NIEs						
	Korea	20,228	25,639	32,678	33,237	20,406
	Taiwan	83,573	92,454	90,310	88,038	83,502
	Hong Kong	42,990	49,250	55,400	63,810	75,320
	Singapore	48,361	58,177	68,695	76,847	122,600*
	USA	74,938	76,656	88,397	—	68,100**
	China	22,387	52,914	75,377	105,000	139,900
	Japan	98,524	125,860	183,250	216,648	219,648

\* Indicates figures of September 1997

\*\* Estimate

Source : Same as Table 1

policies, lower interest rates, gradual industrial restructuring and foreign exchange and capital controls, such as Malaysia and China (including Taiwan and Hong Kong) . The third group switched from rejecting the IMF prescription to adopting it, for example Indonesia. The present situation in Indonesia is rather unpredictable, as the country just held its general elections and the ruling Golkar party (after ruling Indonesia for 34 years) , as generally predicted, lost ground to opposition parties. Both political and economic development in Indonesia, have remained unstable, as the President of the country has yet to be elected and the country's overall reconstruction has yet to be carried out smoothly and speedily.

A simple question that arises here is how can we explain countries in Asia experiencing economic recovery with totally different approaches - either accepting or rejecting the IMF's prescriptions. Has Asia passed its worst period of economic crisis and is Asia's recovery sustainable ? Some sceptics argued that Asia has learnt nothing from the economic crisis and the Asian currencies and stock markets may collapse again anytime.



Incidentally, the Asian stock markets did collapse again, soon after Lee Teng Hui made his 'state - to - state' statement on 9 July. Taiwan's stock markets dropped but experienced some recovery when the central bank in Taiwan interfered. The Asian stock markets have not been further jeopardised as the US, the EU, Japan and ASEAN 10 were quick to re-confirm their 'One - China' policy. The cross strait relations are tense, but at the present time Taiwan is totally isolated. Pressure from Mainland China on Taiwan has been increasing but it is unlikely that the People's Republic of China will unify Taiwan by military means in the near future. The PRC prefers peaceful reunification as long as Taiwan does not proclaim 'independence'.

China, after 21 years of rapid economic development since she first implemented the open door policy in 1978, requires a peaceful environment in the Asia Pacific region to carry on with her fruitful 'socialist market economy'. Besides, in such a severe economic environment in Asia, China has had her hands full, tackling the following problems: diminishing foreign direct investment, decreasing international trade surpluses, restructuring state enterprises, rapid increase of the unemployment rate, income disparity, developmental gap between coastal and inland areas, worsening deflationary tendency etc. China has to solve the above-mentioned problems speedily and regain 7-8% economic growth rate this year before her unemployment problems worsen. In the meantime, China not only has to strengthen its economic relationship with the West (in terms of expanding international trade and luring foreign direct investment and technology) , but also with her neighbouring countries in Asia, particularly the Chinese economies. Chinese economic communities in Asia will in the long run make a notable impact, in terms of capital, technology and managerial know-how, on China's economic development.

It is fair to say that China can claim to be a stabiliser since the financial crisis erupted on 2 July 1997. On many occasions, China was under great pressure to surrender to Renminbi depreciation but managed to maintain a stable exchange rate level with US dollar throughout the Asian economic crisis period. China has therefore contributed greatly, both to the stability of the Asian currencies and to the recovery of the Asian economies.

Obviously, China is a big player in the Asia Pacific arena. However, in terms of economic impact and influence on Asia, one without doubt has to consider Japan with special attention. As an economic superpower and the world's second largest economy, Japan's role in Asia should be properly assessed. As early as in September 1985, due to the phenomenal appreciation of the Japanese currency, Japanese companies started investing heavily in Asia, and this greatly

stimulated economic development of the Asian countries. Both the supply and demand sides among the industries in Asia were prompted by Japanese heavy investment, which had undoubtedly contributed to the creation of the Asia 'economic miracle'.

The bubble economy in Japan burst in early 1991. The Japanese economy has so far not shown any definite sign of bottoming out, despite efforts (deregulation, opening up of domestic markets, financial restructuring, economic stimulus and rescue packages etc.) made by Japan over the period 1991-present. The Japanese economy has been stagnant and the unemployment rate has reached approximately 5%, which is the highest rate since the Second World War.

Asia has long been expecting Japan to recover, the sooner the better. In case of a quick recovery, Asian economies were expecting to be pulled along with Japan, with the aid of Japan's direct foreign investments in the region and Japan's importation of manufactured products from Asia. Japan should have invested heavily in Asia during the 1991 - 1995 period as the Japanese currency continued to appreciate and reached its unprecedented level of 78 yen per US dollar in April 1995. Japan's capital investment in Asia was stagnant, however, during the above-mentioned strong yen period. Besides, the strong yen has also not stimulated exports of manufactured products as expected, from Asia to Japan. Just before the Asian financial crisis in July 1997, exports of manufactured products (machinery in particular) from Asia to Japan had in fact decreased abruptly. Japan's poor economic performance in helping Asia was basically due to her domestic economic sluggishness. To a great extent, the sluggish Japanese economy has contributed adversely to the slowdown of many Asian economies, which has eventually resulted in the eruption of the Asian economic crisis. Asia would not have experienced the worst of the economic crisis had Japan's economy not been in the doldrums till today.

Japan has also been affected seriously by the Asian economic crisis. The following are some of the problems faced by Japan. Asia imports less manufactured products from Japan, Japanese manufacturing industries in Asia are forced to reduce or to stop production, bad debts are accumulated and are not recoverable due to company bankruptcies, foreign debts and loans are not paid due to lack of foreign currency reserves. Japan has been the largest official development assistance donor to the world and to Asia in particular. Japanese banks, financial institutions and private companies, have extended the most debts to the Asian countries, Thailand and Indonesia in particular. Among the highly industrialised countries in the world, Japan suffered the most from Asia during the Asian economic crisis period. The Asian economic crisis has, in fact, postponed Japan's economic recovery.

Economic relations between Asia and Japan are complementary. The New Miyazawa Concept (Shin Miyazawa Koso) planned to distribute some US\$30 billion (which has been increased to US\$800 billion by now) to the Asian countries to help their economies recover. Loans have been extended to some of the Asian countries to develop industrial infrastructure and to nurture supporting industries, to purchase national bonds issued by cash scarce countries in Asia, to settle bad debts incurred by banks and financial institutions in Asia etc. More and more feasibility studies have been carried out and more and more fruitful results are expected. As a substitute to the IMF, the idea that the Miyazawa Concept should develop into the AMF, (Asian Monetary Fund) has yet to be explored. The AMF concept should, in principle, be based on the consensus derived from all the Asian countries involved.

### **Conclusion**

Thai Tom Yam crisis (currency depreciation and stock market collapse) affected not only the ASEAN region but also Hong Kong-a place displaying stability and prosperity. The Hong Kong shock then spread to Japan, Europe and the USA, and then to the whole world. It was termed the Blue Monday of 27 October 1997.

Asia used to have high economic development potential but became the seismic center of the worldwide economic crisis. Korea - as an OECD member next to Japan in Asia, reached a level that without foreign assistance she is not in a position to rescue herself by being self-reliant. Korea received loans amounting to US\$20 billion from the IMF and US\$37 billion emergency loans from the world (essentially from Japan, Europe and the USA) to tackle her economic crisis.

The impact of the Asian economic crisis on Japan is potentially important. Currency and stocks in Japan dropped together with currencies and stocks in Asia. The weak Japanese economy has, in turn, affected the Asian economies quite seriously. Exports from Asia were stimulated due to weak currencies in the region. Exports from Japan to the world have been restricted. Exporting industries in Japan are facing difficulties. However, the weak yen has spurred Japanese exports in recent years. It has not only intensified price competition among the Asian countries but has also had an adverse impact on the recovery of the Asian economies. If the Japanese economy worsens and the yen resumes depreciating, China might have to depreciate her Renminbi in order to stimulate export trade and to attract foreign direct investments. Price competition among the Asian countries is likely to intensify

Japanese enterprises in Asia have also suffered quite seriously during the present economic crisis. It is estimated that more than 3,000 Japanese enterprises have invested in Thailand. The Thai Tom Yam crisis has forced Japanese enterprises to reduce or stop production. Not only Japanese manufacturing industries but also Japanese banks and financial institutions in Asia, and in Thailand and Indonesia in particular, have suffered from millions of bad debts. It partly explains why financial reforms in Japan, since the collapse of the bubble economy in March 1991, have so far not been successful.

Due to the Asian currency crisis, a substantial amount of foreign exchange lost by Japanese enterprises and financial institutions can also not be ignored. The value of real assets held by Japan in Asia dropped drastically (for instance in Thailand, Japanese assets dropped by 30-40 per cent) .

The Asian economic crisis is not a fire on the opposite bank. Japan needs to implement economic reform policies forcefully and decisively under the Obuchi administration, in order to get out from its blind alley as quickly as possible. The Asian economies will not recover easily without recovery of the Japanese economy. A strong Japanese economy is essential for the recovery of the Asian countries.

Japan should initiate bilateral or multi-lateral supportive institutions (for instance through the Asian Development Bank, the World Bank, IMF or some sort of ASEAN Fund or Asian Fund) in order to strengthen cooperation with the Asian countries. Japan is expected to actively participate in mutual assistance, pertaining to Asian economic development, and to extend loans to solve economic crisis problems in Asia. It is crucial for the Asian countries to get out of the economic crisis, as soon as possible, in order to allow the Asia Pacific region to proceed to rapid economic development in the 21<sup>st</sup> century.

#### Notes

1. Nihon Keizai Shimbun-sha-hen, Keizaishingo Jiten 92 Edition,p94
2. Nihon Keizai Shimbun Shasetsu “Indonesia Shien no Jyoken” (conditions for assisting Indonesia) , 22 October 1997
3. Nihon Keizai Shimbun, 27 October 1997
4. Shogaku-kan, SAPIO, 22 October 1997,p23
5. Nihon Keizai Shimbun, 23 June 1997
6. Ibid.

7. The size of USA's GSP increased from US\$3.2 billion in 1976 to US\$10.8 billion in 1983. NIEs constituted 50.8 per cent of the USA's GSP. The breakdown is Taiwan (1st, 24.2 per cent) , Korea (2nd, 12.4 per cent) , Hong Kong (5th, 9.1 per cent) and Singapore (7th, 5.1 per cent) .
8. Keizai Shimbun, 27 July 1997
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10. Keizai Shimbun, 20 October 1997
11. Paul Krugman, "Wrong, It Never Existed", Time, 29 September 1997, p41
12. The Straits Times, 27 June 1997
13. Keizai Shimbun, 16 August 1997
14. Keizai Shimbun, 25 October 1997
15. Keizai Shimbun, 1 August 1997
16. The Straits Times (weekly edition) , 11 October 1997