

THE DEBT CRISIS, AN UNFINISHED BUSINESS: AN EAST ASIAN PERSPECTIVE

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Introduction

1. The perspectives we have from East Asia regarding the recent global financial crisis are coloured by our own regional financial crisis, which affected most of our region a decade earlier. While we recognize a few similarities between the earlier regional and the later more global debt and financial crisis, we also acknowledge significant differences.
2. In our own regional debt and financial crisis, we also faced problems arising from banks and other financial institutions that had overgrown their assets out of proportion to levels consistent with prudential norms; we allowed enormous bubbles to develop and grow; we awoke to our grossly inadequate financial regulatory controls; and we under-estimated the systemic impact on the economy and society from a few financial institutions that all too quickly lost the confidence of financial markets.
3. Unlike the more recent global debt and financial crisis, however, we had the luxury of relative distance from the financial core of the global economy, and of our relative small size within the global financial system, such that the havoc created by our crisis was limited mainly to our region. Moreover, the governments in power in the different economies in the region could take decisive action that needed to be undertaken, admittedly with strong pressure and overwhelming encouragement from the rest of the world.

Lessons Learned from the East Asian Financial Crisis

4. Since we have no effective regional institutions to rely on, as individual national economies, we had no choice other than to undertake the necessary reforms as quickly as possible. We adopted corporate governance principles and best practices quickly; we placed added specific burdens on our banks and other financial institutions, not only in bank governance, but also in

bank supervision, stress testing, and capital adequacy ratios; we introduced reforms to keep our fiscal balances in proper order and our savings rates high; we pushed for intra-regional trade liberalization; and we all started piling up much higher levels of international reserves. How much in all these is of cosmetic value, and how much is of substantive significance would vary from one economy to another: in any case, everything is still work in progress. The facts, however, speak for themselves: East Asia recovered quickly from its regional financial crisis. Within two or three years, most of the economies that had to adopt an IMF-mandated bail-out program were on their decisive way out of the program. We were all eager to pay back IMF bail-out funds as quickly as possible.

5. The governments of each national economy were critical to the speed with which recovery from the crisis was achieved. Despite the variety of forms of government, in East Asia no government suffered from severe constraints in introducing necessary reforms and in going through the proper sequencing of phases to eventual economic recovery: an initial heavy dose of austerity; then, a modest pump-priming in order to quickly re-start the growth engines with a view towards reducing the debt-to-GDP ratio; and once this ratio started to fall, an added boost through more significant, follow-through economic stimulus programs associated with other reforms; continued and sustained efforts at regaining international market confidence, accompanying an effective export drive. Given the relative weakness of other regions of the world, there has been an aggressive push for much higher intra-regional trade, but with investment flows still coming from global financial markets.
6. As our individual economies recovered and got back to their high growth track, with high export growth rates especially to other economies in the region, as well as with reserves being built up to unprecedented levels, we soon became conscious of an East Asian paradox: by the end of the 20th century, in terms of trade volumes and economic growth, we had caught up with the rest of the world; but in terms of regional cooperation and integration as well as with respect to mechanisms to deal with political and security issues within the region, we were still stuck in the 19th century. Our paradigms continued to be shaped by the balance of power syndrome as well as by narrow nationalistic considerations; and the burdens of proximity to each other have been weighing considerably upon all of us. There are many flash points within the region which are crying out for a regional architecture within whose framework these flash points can be contained, and eventually

as well as peacefully resolved. Otherwise, all the gains associated with recovery from the East Asian financial crisis would be thrown away.

The Unfinished Business in East Asia

7. In all economies in East Asia, proper form and appropriate words concerning micro-economic institutional reforms are common. Every economy subscribes to corporate governance principles and global best practices, although fittingly there is much traction for the view stressing the imperative of adapting these practices to the local culture. There is much to commend this view; but behind it also lurks the reticence towards greater openness and transparency, towards more equitable and diligent care for all stakeholders (outside of controlling owners, generally limited to the state or a family), and towards greater responsibility and accountability to regulators and the general public. The corporate governance advocacy in East Asia has a very long way to go; and although an IMF study points to East Asia as having made the greatest strides in corporate governance, the fact is that the region has started from a very low base. It still has a lot of distance to cover to catch up with the more developed regions of the global economy. We never forget that in the immediate aftermath of the East Asian financial crisis, corporate governance reform has been pinpointed as a key area in which--- both in form and substance---significant progress must be made. In terms of form, we have made some progress; but in terms of substance, we need to do much more work. This is very much work in progress.
8. The same is true with the financial system. There has been much progress in adjusting to higher standards of capital-adequacy (relative to quality of assets), the demands of risk management, and strict limits to concentration of assets arising from lending to real estate and a few other sectors. But in many economies of the region, ownership control of banks and other financial institutions is still heavily weighted in favour of families or a network of closely related families, and of the state itself: systemically important banks suffer from issues of directed lending and from concerns over abuses of related party transactions. Moreover, central banks are just beginning to acquire greater autonomy and independence from other instrumentalities of the state. While concerns about regulatory capture even of central banks and other supervisory authorities (including such self-regulatory organizations as the stock exchange) have been eased to some extent, still those concerns do have some basis in a number of East Asian economies. There has also been progress towards setting up regional

financial support mechanisms in times of liquidity emergencies, such as the setting up of the Chiang Mai initiative; nonetheless, the amounts put in have been modest, and the mechanism has yet to be tested in a real (not just simulated) emergency. Regional initiatives towards setting up a regional bond market have been bruited about and discussed for years; but they have to succeed, and the region is still faced with few options other than funnelling its considerable reserves to more developed financial centers and to Treasuries in more advanced economies. While the region has significant financial resources to match its equally significant financial requirements such as for public infrastructure investments, still it continues to rely on financial markets, mainly outside the region, to do the matching between supply and demand. Dependence on global financial flows, particularly of investment flows, has not diminished, and regional vulnerability to developments in global financial centers has not been moderated either. This represents a huge unfinished business, which keeps the region as a largely passive player in initiatives to build a more robust global financial architecture.

9. Given the relative centrality and importance of governments in the polity, economy, and society of East Asia, an even bigger unfinished business is the alignment of public governance practices with global best practices. Corruption remains a big question mark; the “rule of law” is still looked at as a Western imposition in a region where the preference is the “rule by law” on the part of those who happen to have the reins of power. While hundreds of millions of people have been pulled across the poverty line in East Asia in the past 3 decades (mostly in China, but not limited to China) through the broad process of economic liberalization, there has not been an equally impressive advance in political liberalization nor in social participation open to ordinary citizens: the ruling elite continue to dominate with almost undiminished influence and power. This may have conferred significant advantages in enabling governments to take decisive and quick action in the face of crisis. But over the long-term, given the ever-higher demands of sustainability, key questions arise on the status quo and on critical steps that need to be taken towards a more systemic and therefore comprehensive, balanced opening up not only of the economy, but also of the polity, and of society as a whole. Those key questions are begging for answers.

Unanswered Key Questions

10. East Asia, on the whole, has shown smart pragmatism in confronting the financial crisis of the region more than a decade ago and in absorbing the negative impact on its constituent economies arising from the more recent global debt and financial crisis that started five years ago. Recovery was relatively quick from its own regional financial crisis; but there has been some slow-down in economic growth arising from the more recent global financial crisis. Some key reforms have been undertaken, at least in form, but also gradually and more hesitantly in substance. But moving forward, most East Asian economies have yet to address the key question concerning the centrality of individual persons. They (the East Asian economies) still tend to look at individuals more as means rather than as ends of the policies of the state: where they can be used as assets, individuals are exploited; but where they are looked down upon as liabilities, the attitude is to marginalize them, or even to remove them from the radar screen. The enormous demographic challenge this poses for the future of East Asian economies is too daunting to think about. Nonetheless, some practical steps need to be taken in the immediate future. What those steps are can become clear from straightforward answers to the key question of individual personal dignity.
11. A related unanswered key question is the importance of intermediate institutions in society. East Asian societies are family-oriented; all profess the importance of the family; but in practice, in some economies, marriage is going out of fashion, while consumerist lifestyle preferences are given much higher priority than the provision of a bigger base for future generations. Greed for material leisure and personal convenience takes precedence over selfless sacrifice for others, particularly the children that God may send. Moreover, schools are regarded as factories for heavily stressed students under extreme pressure to get to the best high schools, the best universities, and the best jobs. Civil society organizations are looked upon with critically discerning and deeply suspicious eyes. Indeed, the key question concerning the role of intermediate institutions in society to give substance to subsidiarity and the flowering of diversity and initiatives in society remains up in the air. In the meanwhile, the “bureaucratic state” takes a heavy toll on the full and balanced development of individual personalities.
12. With only a few exceptions, there can be no doubt about the effectiveness of a central authority that governments enjoy as the main coordinator and promoter of the common good of society. But governments face limits: where discretion is unchecked, corruption rears up its ugly head; where transparency is honoured more in its breach, prerogatives and privileges are

easily abused; where greed for material luxuries and the accumulation of wealth and power faces few effective restraints, selfish interests soon precede the many demands of the public welfare. The key unanswered question concerning the limits on the power of government revolves around the balance between effectiveness and just due process. Doubtless, central authority has to continue to be strong and effective; but every possible guarantee should also be taken to ensure that its exercise is mainly, if not exclusively, for the common good of all, with all due respect for the basic human rights of individual citizens and the primary rights of basic intermediate institutions.

Concluding Comments

13. The debt and financial crisis that we in East Asia went through before the turn of the last century highlighted a basic truth about where we stand in the world. In terms of trade and economic growth, we have found a way towards claiming a much heavier weight in the global economy. But in terms of financial flows as well as in architecture to deal with regional political and security issues, we are very far behind. It is of no surprise, therefore, that on issues concerning the technical aspects associated with a global financial architecture, which can deal more effectively with global financial issues, we tend to follow global initiatives and act on them quickly. Moreover, we tend to link the resolution of critical financial problems with rapid export growth, increasingly through the exploitation of intra-regional trade opportunities.
14. The main concern in East Asia, therefore, is how to create mechanisms that would further expand intra-regional trade. On our agenda is a framework for a comprehensive economic partnership as well as for a trans-pacific partnership. We also have initiatives to launch an ASEAN economic community in the foreseeable future, and there are visioning exercises for an East Asian community (with special emphasis on the small “c” in community, rather than a capital “C”). And while we have an alphabet soup referring to other initiatives for regional confidence-building and for securing “peace and tranquillity” in the region, still the operational focus remains on the area where we can make the most significant progress, i.e. in intra-regional trade. While we are convinced we can continue to make more progress by focusing on intra-regional trade, we also are aware of the systemic inter-connection between trade and finance in the economy as well

as the close inter-connection between economic growth, financial and political stability as well as social progress. The East Asian financial crisis taught us unforgettable lessons on these inter-connections: it is mainly for this reason that we connect debt and financial crisis with the wider issue of trade, continuing reform, and regional community-building. Thus, we are trying to apply those lessons to the more comprehensive efforts at building an East Asian community and determining the positive role it should play in the global community.

15. Under this light, we now are working on the foundations of an East Asian community. What should its identity be? What are the core values that should serve as its foundations? How should it play a positive and constructive role in the world? What mission in the global community should it seek to undertake such that instead of being a burden to the world, we become not only the region with the heaviest weight in the global economy but also one of its more politically constructive and socially responsible regions. We need inspiration and clear guidance as well as strong encouragement and effective support as we navigate through these game-changing issues, where important breakthroughs have to be made to help secure the peace and progress of the entire human family.

Manila, September 2013