



Asia in the Light of the Financial Crisis

By Dr Richard Grant, Executive Director Asia New Zealand Foundation

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First of all, let me say that I am not an economist. Nor am I a prophet.

That means that I am giving you some personal views, about things and issues in the current financial scene which strike me as relevant to New Zealand.

I have some slides which I've picked from various places and websites to try and give a picture of the international crisis. Then I want to talk about whether and/or how Asia is affected by the crisis. And then see if there are any pointers for New Zealand as a result.

I think we can all understand something of what has happened in the global economy, starting in the US and spreading out from there. If at first people were reasonably confident that their own country would escape some of the consequences of the turmoil, it is clear that day by day, week by week, the evidence has been other.

Table 1. World economic forecasts.

Source: ANZ Economic Outlook 15 October 2008

GDP growth (%)	2007	2008(f)	2009 (f)	2010(f)
Australia	4.2	2.3	1.8	1.9
New Zealand	3.2	0.7	0.5	2.5
United States	2.0	1.5	0.7	1.7
Euro zone	2.6	1.1	0.6	1.7
Japan	2.0	0.6	0.7	1.6
China	11.6	9.7	8.0	8.9
Other East Asia (Excl China & Japan)	5.9	5.1	4.8	5.6
India	9.0	8	7	7.7
World (PPP)	4.8	3.6	2.9	3.8

Table 2. OECD growth forecasts – annual % change in real GDP.

Source: *Financial Times*, November 2008

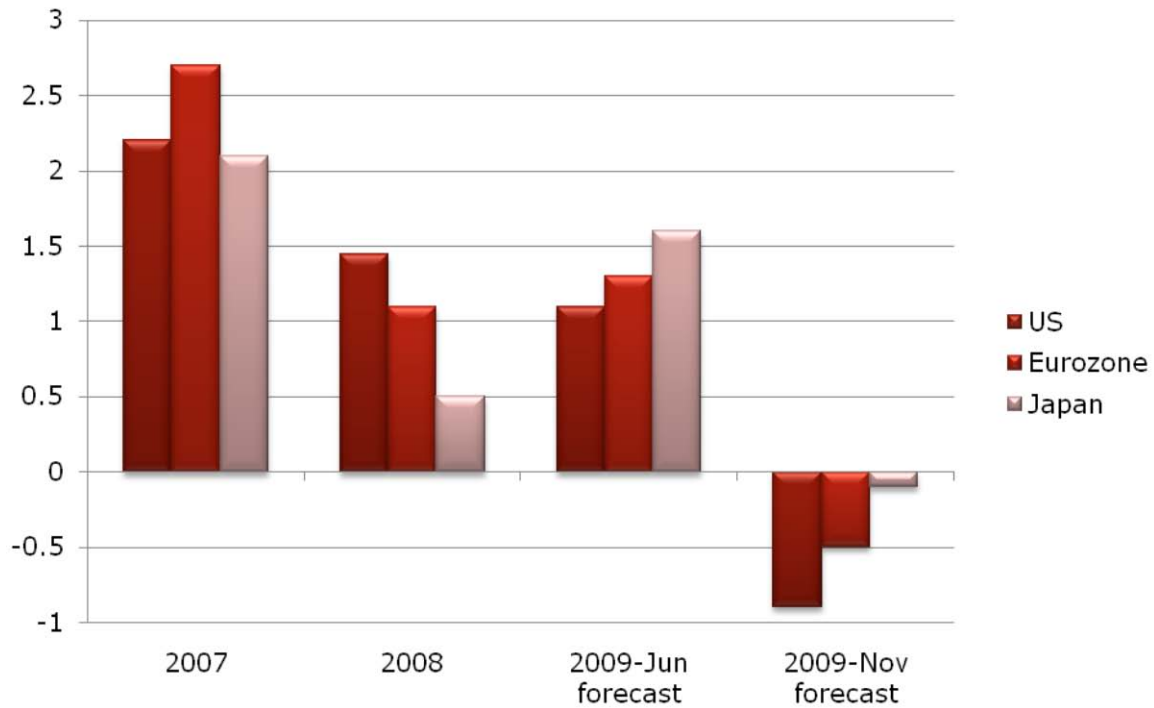


Table 3. Financial rescue plans.

Source: *Financial Times*, October 2008

Economy	Amount
US	\$1,500bn
Germany	€515bn (\$645bn)
UK	£400bn (\$590bn)
France	€360bn (\$450bn)
Netherlands	€200bn (\$250bn)
Russia	\$210bn
Sweden	SKr1,500bn (\$190bn)
South Korea	\$130bn
Austria	€100bn (\$125bn)
Singapore	S\$150bn (\$100bn)

Just to give some examples, in addition to the ones which are well known to you:

- the stock market in Saudi Arabia has declined by 60% since the beginning of the year – its capitalisation has dropped by \$US180 billion
- Singapore and Hong Kong are in recession
- If you want to charter a bulk carrier, the daily rate has dropped from \$US230,000 to \$US9000 in just the last two months
- The global hedge fund industry lost \$US100 billion in assets in October alone
- Iceland is bankrupt
- Indian motor cycle sales (a better indication of the strength of the economy than car sales) dropped 18% in October 08 over October 07.

Looking at Asia

Table 4. Asia: Real GDP Growth (year-on-year % change).

Source: *Regional Economic Outlook – Asia and Pacific*, IMF, November 2008

Economy	2007	2008	2009	2008	2009	2008	2009
		Latest projections		Difference from October WEO		Fourth Quarter*	
Industrial Asia	2.4	0.8	0.1	-0.2	-0.6	0.0	0.6
Japan	2.1	0.5	-0.2	-0.2	-0.7	-0.3	0.4
Australia	4.4	2.4	1.8	-0.1	-0.4	1.8	2.0
New Zealand	3.2	0.7	1.5	0.0	0.0	0.0	1.5
Emerging Asia	9.5	7.7	6.5	-0.1	-0.8	6.8	6.8
Hong Kong SAR	6.4	3.7	2.0	-0.4	-1.5	1.0	4.4
South Korea	5.0	4.1	2.0	0.0	-1.5	2.4	3.7
Singapore	7.7	2.7	2.0	-0.9	-1.4	1.6	4.4
Chinese Taipei (Taiwan)	5.7	3.8	2.2	0.0	-0.3	2.5	5.6
China P Rep	11.9	9.7	8.5	-0.1	-0.8	9.0	8.3
India	9.3	7.8	6.3	-0.1	-0.6	6.6	6.0
ASEAN-5	6.3	5.4	4.2	-0.1	-0.7	4.6	5.4
Indonesia	6.3	6.0	4.5	-0.1	-1.0	5.4	5.1
Malaysia	6.3	5.7	3.8	0.0	-0.9	4.7	4.4
Philippines	7.2	4.4	3.5	0.0	-0.3	3.9	3.6
Thailand	4.8	4.5	4.0	-0.2	-0.5	2.6	6.3
Vietnam	8.5	6.3	5.5	0.0	0.0	7.5	8.0
Emerging Asia excl. China	7.3	5.9	4.4	-0.1	-0.8	4.7	5.3
Emerging Asia excl. China, India	5.9	4.6	3.1	-0.1	-0.9	3.4	4.9
ASIA	7.6	6.0	4.9	-0.1	-0.7	5.1	5.3

* Change from fourth quarter of preceding year

In this continuing turmoil on both financial and economic fronts, one issue I want to raise is the argument about the link between Asian economies and the rest of the world, and more precisely with the United States.

Table 5. Percentage contraction in GDP for each one percentage contraction in US GDP (median for the region).

Source: Mastercard Worldwide Insights

	1974-1975	1980	1982	1991	2001
Other industrial countries	0.89%	0.44%	0.09%	0.62%	0.69%
Emerging Asia	0.57%	0.09%	0.33%	0.05%	0.38%

A tremendous amount has been written about this, by people far more knowledgeable than me. To reduce the proposition to a soundbite, the debate has been about whether the Asian economies have developed sufficient strength and resilience over the last decade to be less affected if the US were to go into recession.

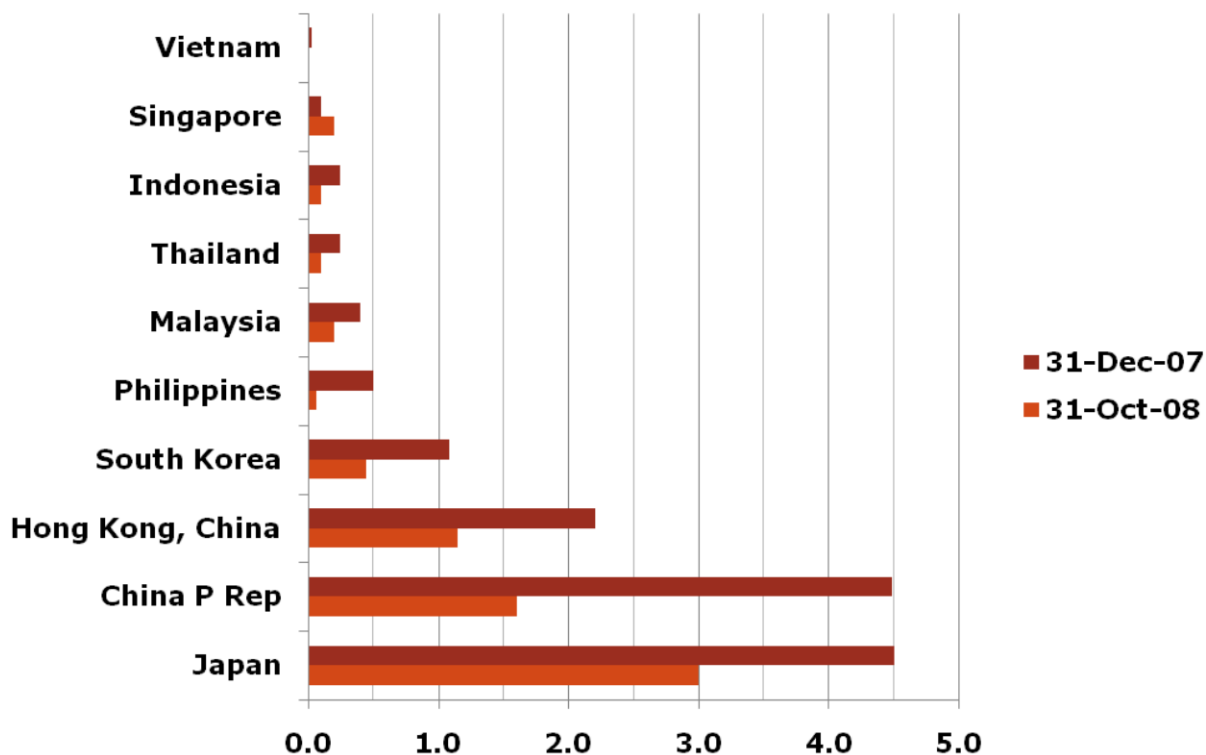
The question is whether Asia can continue to grow and prosper in the event that the US has a downturn – as it has. Has Asia, in the jargon, “decoupled” from the United States?

Decoupling has been defined in the following way by researchers at the Hong Kong Monetary Authority in a working paper in March last year. To be decoupled, Asian economies should have:

1. exports sufficiently diversified to markets other than the US;
2. the setting of monetary policy sufficiently independent of the US; and
3. Financial markets in Asia sufficiently uncorrelated with US markets (See Table 6 on the following page)

Table 6. Emerging East Asia equity market capitalisation (US\$ trillion)

Source: *Asia Bond Monitor*, Asian Development Bank, based on Bloomberg data



That is a fairly tight definition, and on the face of it, one would have to say that Asian economies – as we look at them today – have not decoupled from the US.

Exports will drop, including to the US (although in the case of India, the EU is a more important market than the US.)

Table 7. ASEAN's trade with the US (US\$ million)

Source: based on data from US-ASEAN Business Council

	2000	2007
US Exports	47,140	60,562
US Imports	87,945	111,170
TOTAL	135,085	171,732

Table 8. China's trade with the US (US\$ billion)

Sources: US-China Business Council based on data from US International Trade Commission, US Department of Commerce and US Census Bureau

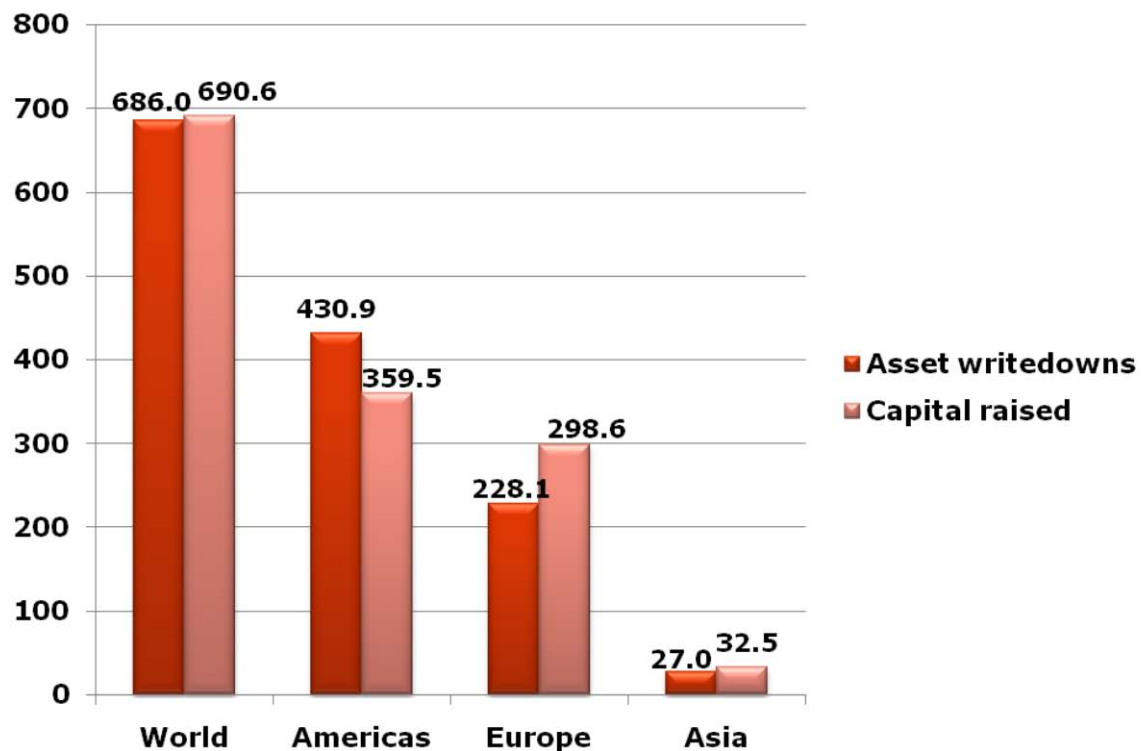
	2000	2007
US Exports	16.3	65.2
US Imports	100.0	321.5
TOTAL	116.3	386.7
US Balance	-83.7	-256.3

Monetary policy is not "sufficiently independent" of the US to see Asian currencies strengthen with the exception of the yen and possibly the yuan. In most cases the US is currently strengthening against Asian currencies.

And financial markets in Asia are in decline, although this decline not as severe as the US.

Table 9. Bank writedowns and capital raisings by banks since the 3rd quarter of 2007.

Source: Asia Bond Monitor, Asian Development Bank, based on Bloomberg data



And, of course, the simple deduction is that, in a globalised economy, it is hard to see that any country participating in it can escape the consequences of what is going on around the world.

The IMF, for instance, has reduced its estimate of global growth in 2009 from 5.4% to 2.2 % in a very short time frame. Asia will drop from 7.6% last year to 4.9% next year.

Ominously, Robert Zoellick, the President of the World Bank, said earlier this month that global trade would shrink next year for the first time since 1982. And there is a question of availability of trade credits affecting the Asian region as it does other regions.

On the decoupling issue, others use different arguments, largely based on the percentage of net exports in the trade of Asian countries, which are generally low, and are, therefore, not so susceptible to a slowing down of the US economy.

Table 10. Net exports as percentage of real GDP in 2006

Source: Mastercard Worldwide Insights

China	7.5%
Japan	0.8%
India	-0.7%
Indonesia	1.4%
South Korea	1.6%
Malaysia	0.0%
Philippines	4.2%
Taiwan	3.6%
Thailand	4.8%

Table 11. ASEAN: intra- and external trade (US\$ billion)

Source: Chinaview.cn

	1997	2007	% change
ASEAN external trade	548	1,200	118.7
Intra-ASEAN trade	150	403	169

And there are a few voices which suggest that Asia is now sufficiently strong to stand on its own feet, despite the recession in the US. Here is Kishore Mahbhubani, a former Singapore Ambassador and currently Dean of the Lee Kuan Yew School of Public Policy, in an article in the *Financial Times* at the end of October:

“The really good news is that few Asians have lost their optimism about the future. They have no illusions about the crisis but are confident that they remain on the right trajectory to deliver the Asian century. This is why the key Asian economies will react calmly in this storm. Confidence in the future is a great asset in such times.”

What has happened in Asia?

Growth rates have been sharply scaled back.

Emerging Asia equity markets have fallen by about 50% since the beginning of the year.

India expects GDP growth in 2009 to drop from 9% to 7% in the government's estimates, but think tank economists to whom I spoke in Delhi a couple of weeks ago consider that the Government is on the optimistic side.

China has dropped from 9.5% to 7%, and has as you know introduced a \$586 billion stimulus package.

Japan has slipped into recession, and even the Government – again on the optimistic side – expects growth of only 0.1% in 09.

Korea's 2009 growth has shrunk to only 2%.

Taiwan is predicted to reach only 1.3%.

Thailand will reach 3.8% according to the Central Bank.

And so on, across the Asian region. So, looking at the overall picture, it becomes clearer that decoupling seems to be implausible

What does it mean for Asian countries?

With these sorts of growth figures, it is not surprising to see accompanying stories of rising unemployment; falling tourism figures; contraction in mergers and acquisitions; and difficulties for people newly entering the labour market. In other words, Asian countries are facing the same sorts of problems as we are in New Zealand.

The news is not encouraging. Probably the only encouraging news is that most Asian countries are, first of all, much better placed than they were during the last Asian financial crisis 10 years ago; and that they are relatively better off than Western Europe and the US.

Table 12. Asia: Official foreign exchange reserves (US\$ billion, end-period)Source: *Regional Economic Outlook – Asia and Pacific*, IMF, November 2008

Economy	2006	2007	2008 October*
Industrial Asia	964	1,018	1,021
Japan	895	973	978
Australia	55	27	29
New Zealand	14	17	15
Emerging Asia	2,477	3,259	3,628
Hong Kong SAR	133	153	161
South Korea	239	262	212
Taipei, China	266	270	278
Singapore	136	163	162
China, P Rep	1,073	1,534	1,912
India	177	275	258
ASEAN-5	226	301	322
Indonesia	43	57	51
Malaysia	82	101	110
Philippines	23	34	36
Thailand	67	87	102
Vietnam	11	21	24
Emerging Asia excl. China	1,405	1,725	1,716
Emerging Asia excl. China, India	1,228	1,450	1,457
ASIA	3,442	4,277	4,649

* October data - except for the following countries, for which data end in September: Australia, China, Hong Kong SAR, New Zealand, and Vietnam.

Table 13. Stock of foreign direct investment - inbound and outbound (US\$ billion, 31/12/2007 est.)

Source: CIA World Factbook

Country	FDI inbound	FDI outbound
Japan	110.8	533.1
China	758.9	93.75
South Korea	119.6	82.1
Malaysia	86.16	42.55
Singapore	214.5	111.2
India	95.96	37.5
New Zealand	71.31	N/A

On the positive side, it is clear that the crisis does present an opportunity to put in place policies which may make economic growth in the future more likely and more significant.

Almost all governments have taken measures to increase liquidity in their markets and banking systems.

Infrastructure development funded by Government stimulus packages, for instance, could well produce positive outcomes. In India alone, for instance, the estimates are that just to keep industry supplied with sufficient energy to grow will require a **ten-fold** increase generating capacity over the next 5 years.

Secondly, the crisis is leading to falling inflationary pressures across the region.

Commodity prices are easing. The fall of the oil price is beneficial to those who consume it, but not good for the books of those who produce it (Indonesia, Vietnam, Thailand).

Table 14. Crude oil prices

Source: *Financial Times*



\$147 per barrel

(July 2008)



\$50 per barrel

(25/11/08)

There are indicators that Asian financial institutions are, however, using their capital reserves to invest in the US and Europe – so there is some judicious investment going on which should bear fruit in the future.

Trade pressures will affect these countries significantly. Goods and services exports are expected to slow down. India, with less of its economy exposed to global markets, may be better placed than some others, although its services sector expects some serious disruption – shipping, IT systems, in particular.

China, through its stimulus package, is trying to increase domestic demand to compensate for reduced export demand. Vietnam will be facing a similar position.

One of the questions which will arise is the role which sovereign wealth funds will play in re-building corporate structures around the world.

Table 15. Sovereign wealth funds of Developing Asia.

Source: *Capital Outflows, Sovereign Wealth Funds and Domestic Financial Instability in Developing Asia*, ADB Economic Working Paper series, October 2008

Economy	Name of Fund	Assets (US\$bn)	Year of inception	Type
Singapore	Government of Singapore Investment Corporation	330	1981	Noncommodity
China, P Rep	China Investment Corporation	200	2007	Noncommodity
Singapore	Temasek Holdings	100	1974	Noncommodity
Hong Kong, China	Investment Portfolio (HKMA)	100	1998	Noncommodity
Brunei Darussalam	Brunei Investment Agency	30	1983	Commodity: Oil
South Korea	Korea Investment Corporation	20	2005	Noncommodity
Malaysia	Khazanah National BHD	15	1993	Noncommodity
Kazakhstan	National Oil Fund	15	2000	Commodity: Oil, gas, metals
Taipei, China	National Stabilization Fund	15	2000	Noncommodity
Azerbaijan	State Oil Fund	1.6	1999	Commodity: Oil
Timor-Leste	Petroleum Fund	1.22	2005	Commodity: Oil and gas
Uzbekistan	Fund for Reconstruction and Development	0.5	2006	Commodity and noncommodity
Kiribati	Revenue Equalization Reserve Fund	0.47	1956	Commodity: phosphate mining
Nauru	Nauru Phosphate Royalties Trust	0.07	1968	Commodity: phosphate mining
India	To be named	n.a.	n.a.	Noncommodity
Thailand	To be named	n.a.	n.a.	Noncommodity

US carmakers might not be a good bet: major Western banks will be patchy. But re-capitalisation is needed, and Asia has a lot of money.

What does it mean for the international system?

The blame game. This was all the fault of greedy Wall Street and other Western markets. Obviously, there is truth in that. What did Greenspan call it? "Irrational exuberance". Well, the bubble finally burst.

Yet there are commentators who point out that people other than the US and some developed countries fuelled the expansion of credit. Asian countries, with their large surpluses, are amongst them. And the expansion of the Indian and Chinese economies were in no little way funded by their growing access to global trade and their growing access to inbound investment.

Clearly the global financial system is going through a period of stress such as we have not seen since the great depression. This means, incidentally, that there is no-one around in a position of influence who experienced what happened then, and, of course, none of us under 65 have experienced anything like it. So perceptions and reactions are coming from people seeing these things happen to them for the first time. This is not an easy climate for public policy makers.

Right now, we have had two major meetings in the space of the last fortnight which have directed their attention to the crisis. The G20 meeting in Washington on 14 and 15 November, and the APEC meeting in Lima last weekend.

Clearly, the G20 meeting, bringing together more countries with an interest in solutions around the table, is the first major step. Commentators are dismissive of the G7 – with some justification. And the G8 with Russia included does not do the trick either.

Some reform of the global financial institutions and what they do, including their governance, is necessary, and inevitable. This was one of the key decisions in Washington. The proof of the pudding will be in the eating. But, a system which does not include, as of right, China and India, to take two major Asian powers, is obviously not sustainable.

The second key message out of Washington was a rejection of protectionism in both the financial and trade fields. The talk is of an "ambitious outcome" for the Doha Round.

And although one feels a certain *déjà vu* at these sorts of statements, it is important that things are starting to happen, because if there has been the sort of reaction by individual national governments such as there was in the 1930s, the consequences would have been much grimmer.

APEC has issued a communiqué which says, inter alia:

The current global financial crisis is one of the most serious economic challenges we have ever faced. We will act quickly and decisively to address the impending global economic slowdown. We welcomed the monetary and fiscal stimulus provided by APEC member economies and will take all necessary economic and financial measures to resolve this crisis, taking the necessary actions to offer hope to those most in need. Our resolve to address

the deteriorating global economic situation, and support a prompt, ambitious and balanced conclusion to the WTO Doha Agenda (DDA) negotiations, is outlined in a separate statement [which called for Trade ministers to meet in Geneva in December].

What does it mean for New Zealand?

New Zealand is facing an Asian region which is in some stress. If anything, the crisis probably drives us nearer to Asia than we might have expected. Why is this?

First, our export trade is now more Asia-centric than ever: 10 of our top markets are in Asia, and, even before the crisis, our share in the growth of Asian markets was stagnating.

Second, inbound tourism from around the world is down, and significantly also from Asia. The latest statistics show a year-on-year drop of 32% from China, 17% from Korea, and 15% from Japan. If tourism stays low from the UK, US, and Europe, there will have to be a decision about where we can re-stimulate growth, and if Asian economies come out of the slide more quickly, I would argue that we should be doing more to attract tourists from there.

International students, particularly those from China and Japan, have also fallen in recent times. So in our major service sectors we have a challenge.

Generally, if the downturn in OECD countries is more severe than in Asian countries, which looks likely, it is important that we decide to do better in Asian markets, for both goods and services.

Third, the downturn will correct, and it is clear that countries in Asia will be focussed on growth. The immediate future may look a bit glum, but when the global economy starts to pick up, Asian growth will be important.

Thirdly, we have been able through successful diplomacy to gain a place at the table in the region. We have long been a dialogue partner for ASEAN. We are now a member of the East Asia Summit. We have free trade agreements with China, with Singapore, with Thailand, and with ASEAN, negotiations in play with Malaysia, plus a study under way with Korea, and about to come with Japan.

These are advantages which we have in place. We should be thankful we got them in place before the crisis hit. It will be much harder for others to negotiate these sorts of agreements in the reigning economic climate.

Clearly, a kick start to the MTN with a speedy and liberalising conclusion would be great for New Zealand. It is encouraging that both the G20 and APEC said so. Progress will not depend so much on what New Zealand says and does, but what much bigger economies including our Asian partners say and do, will be critical. So we should make use of our relationships in the region to urge them on.

Finally, coming back to the ongoing discussions about our role in the emerging architecture in East Asia, it seems to me that the crisis has shown us that we are more part of this region than we thought we were. It is in our interests that Asian countries have a better place in the institutions that are going to be reformed as a result of the crisis. Their economic growth is more important to New Zealand than ever. The last Asian crisis in 1997 was not seen by many in New Zealand as really affecting us. This time it is different. Acknowledging that is a big step forward.