Good evening.

When you try to transform a tight, feudalistic society, such as you have in Asia, into a modern, capitalistic society—much as you have in the West—you run into a lot of trouble. In Asia now, almost every aspect of the society and economy is being overturned by large, impersonal forces—called the market. In the short run, it’s going to be very tough for the region, but I assure you, in the long run, it’s the best thing that can happen.

Though Asia grew very rapidly over the last three decades—East Asia, at an average of 8% a year—the growth was not, in some sense, very sound. It was lopsided, depending almost exclusively on exports, and it was ultimately inefficient, allocating resources based on relationships rather than rates of return. The system worked as long as there wasn’t much competition or foreign pressure; but now that these things are intense, it’s failing. In the long run, with fundamentals like a high domestic savings rate, prudent monetary and fiscal policies, a dynamic private sector, relative openness to trade, a commitment to training and education, Asia will be okay. The challenge is to get rid of the negative parts of the political and social structure that obscure these very real strengths.
But it won’t be easy. Too many people, with too much power, are still enjoying personal prosperity, so any fundamental change is going to be resisted—fiercely. As we already see, the elites will hold on to the very end, no matter how much their countrymen suffer in the process. Even in Japan, you have a bureaucratic class whose interests are now divorced from those of the country.

Now, why did Asia fall so quickly? Why did it go from boom to bust in the blink of an eye? In technical terms, it was a maturity mismatch between borrowing short term and investing long. For instance, of Thailand’s total debt of $92 billion by August 1997, $35 billion was short term. Also, it’s a currency mismatch: borrowing in foreign currencies without sufficient foreign exchange to repay it. Additionally, there was poor credit risk and banking supervision, and a totally prostrate legal system. In Thailand, where the crisis began, this exposed other weaknesses, such as large, unhedged foreign borrowing by the private sector, an inflated property market, and a weak, over-extended banking system. As Thailand’s currency plummeted, improving its own export competitiveness, it pressured the currencies of its neighbors, leading investors to look at them more closely and seeing the same problems, to lose confidence. Debt matured all over the region, and it was largely unpayable.

While it’s hard to generalize about Asia, with its many societies, there is a common core; above all, corruption. Second, a lack of total transparency—in the sense of openness and no duplicity. Third, capitalism without safeguards. In a way, though, you can’t really blame them, because for hundreds if not thousands of years, oriental society has existed on a certain tacit understanding of things, which is very different from the Anglo-American way of thinking. Since you’re dealing with basically the same peoples in the same area for such a long period of time, there’s a kind of unwritten, unspoken understanding of how things work, what is required, and so
on. This quietude is definitely an Asian ideal, considered beautiful. But with the advent of the
markets, these ties are going to melt; things are going to become explicit; contracts are going to
replace silent understandings. The markets, in certain ways, are going to make Asia look more
like the West—especially America.

Now, enter the International Monetary Fund—so much in the news of late. Is it the savior
of the Asian economies, a white knight to the rescue? Or is it an American Trojan horse, intent
on humbling its all-too-successful competitors?

I think the IMF programs are the perfect prescription—if only because if followed, easing
the path to market economies, they’ll spare Asia a lot of pain later on. The markets certainly like
them: in Indonesia’s case, after the IMF program was announced, the rupiah strengthened 5% in a
day and the stock market 10% in two. Most economists like them too. Now, if you’re an Asian
traditionalist, you’ll probably see these programs as the destroyer of long-held practices and social
arrangements, leading to every conceivable difficulty at home and in foreign policy. I’m not
prepared to say who’s right and who’s wrong. They’re all right and they’re all wrong to some
extent. Anyway, to me it’s a sterile argument. Instead of moaning about the nasty IMF, the
austerity, the coming foreign tide, the Asian just ought to accept reality and ask themselves, where
do we go from here?

The answer is simple: liberalize. Open your markets; increase transparency and the data
flow; tighten your regulation; spend wisely; provide a social safety net; hold open elections; fortify
the legal system; increase competition; end cronyism. In other words, maintain policies that the
markets like, and they will reward you; “investor confidence” is the new international
disciplinarian. To too many Asian ears however, this smacks of Western imperialism. It isn’t, of
course—it’s just smart governance—but it’s this feeling, this irrational feeling, that’s keeping Asia back—penalizing it in global markets.

To Asia, for the meanwhile, I say: don’t fight it, just do what you have to do! And to the IMF I say: be tough, especially in places like Indonesia, where in order to liberate the economy you have to break the stranglehold of the elites. No reform, no money! In the long run, Asia has to find a way of reconciling its society and economy to market forces …

Whether desired or not, technology is compressing the globe. For money, it’s completely one global market. Capital skips from place to place. The futures, derivatives, foreign exchange markets are now a hundred times larger than actual supply and demand. This introduces a speculative element, where success is greater but also the risk. You need a certain level of sophistication and experience—lacking for the most part in Asia—to handle these things. If you don’t have it, you shouldn’t get in the game; but then you lose out on needed capital. It’s an iron-clad tradeoff.

We all tap the same equity and debt markets; therefore, we all end up using the same yardstick. And again, whether you like it or not, that yardstick was made in America. Because of the depth of their markets and the strength of their governance, the Anglo-Saxons are totally dominating the global financial system.

Now, it is true that till quite recently, people were pouring money into Asia. In an article a few months ago in The Washington Post, Henry Kissinger said that “Cronyism, corruption, and weak, non-transparent banking systems were widespread. But until last summer, these were treated by what were the largest and most sophisticated lenders and investors in the world as tolerable risks, not obstacles to lending.” That’s not quite true. The most sophisticated investors, like a George Soros, didn’t like what was going on and got out early, or betted against the
currencies. Most of the other money—at a rate, for instance, of 17% of Malaysia’s GDP in 1993 and 13% of Thailand’s in 1995—was coming from banks and other lenders who, less astute, misconstrued events there. Once they learned, they panicked. The thing now, to Asia’s detriment, is that in an open, global economy abetted by high technology, money is very sensitive and hot-footed.

Let me be clear about something, however. I don’t think all the Asian economies are equally sick—not by any means. It’s fair to say that Taiwan, Singapore, and Hong Kong are still doing quite well. And that Indonesia is doing by far the worst, followed by Malaysia, then Thailand, then Korea. Between December 1996 and February 1998, Taiwan’s stock market increased by 12% in dollar terms, while Indonesia’s fell over 80%. The extent to which these economies are healthy or sick is the extent to which they obey the dictates of the market.

Indonesia, as I’ve indicated, is very precarious. This year its GDP is expected to contract by 5.2%. Yet the autocrat Suharto is hanging tough, twisting and dancing his way out of IMF reforms. It’s tragic, really. He’s so isolated by his money and his cronies, by his long and militarily enforced tenure, that he doesn’t hear the pain of his people—and wouldn’t care if he did. Indonesia is just the epitome of malignant misgovernment.

Both Indonesia and Malaysia have a potential blood bath on their hands with this split between the preponderant Malays and the economically dominant Chinese. Malaysia has now wisely agreed to let the ethnic Chinese help bail out floundering Malay conglomerates, though that’s not enough. The Chinese must somehow show their patriotism—felt or not. They mustn’t be seen as avoiding the suffering that will visit the Malays. If the Chinese, with their mobile capital, profit from a restructuring while the Malays suffer, that’s a recipe for slaughter.
In Korea, though the problems are very deep (in December, before the IMF stepped in, short term debt reached 14 times its foreign reserves), the prognosis looks a little better. They have the right man, Kim Dae Jung, as president. An idealist, one who has faced death several times for his beliefs, he has the stature, the moral authority, to move the country in the right direction. He’s left of center rather than right; smart and tenacious; above all, unafraid to tell the truth. At a sort of town meeting in Korea in January—an unprecedented event there—when asked whether foreign investment meant the “economic colonization” of Korea, he told it straight: “We must accept a lot of foreign investment … When money enters my country, that’s my money. Times have changed so that we are living in an era in which gaining foreign investment is more important than boosting trade … We’re living in a globalized economy, and in this respect our country is very backward … If foreigners think [we are very rude to them], then no investment will enter Korea, no tourists will come here, and no one will buy our products … How can we survive like this?” At first stunned, the audience broke into long applause. I must say that as a native Korean, though a long-time U.S. citizen, I’m very hopeful and proud.

Though the sailing won’t be smooth, Korea has come to a consensus that it must reform—that it must overhaul a system in which the top 30 chaebol had an average debt-to-equity ratio of 400%, compared to 70% in the United States; in which because of opaque accounting, short term debt was understated by at least $35 billion. I think that because it’s committed to restructuring, IMF style, in three to four years Korea will be very healthy again—in fact, a genuine competitor to Japan.

Now a good question is, why are Taiwan and China, and to some extent Singapore, sitting out this crisis? Is there a special “Chinese” factor? I don’t think so. There are unique reasons for their success.
Compare Korea and Taiwan’s development. Korea went the conglomerate route, concentrating on heavy industry and chips; Taiwan took to small and medium-size companies, sticking to parts and assembly. These, concentrating on profits, beat the conglomerates, which were fixated on accumulating assets and market share. The result? While Korea’s economy should contract by 2-3% this year, Taiwan’s is predicted to grow by 5%. Also, as *The New York Times* pointed out recently, Taiwan’s political isolation may have been, ironically, a blessing in disguise: if they messed up, no one was around to save them. They *had* to succeed, which meant obeying the markets, the *logic* of the markets. With over $80 billion in foreign reserves, healthy industry, and a conservative banking system, they’re in very good shape.

Singapore is different. It’s run by a dictator, Lee Kuan Yew. He’s a dictator to be sure, but a shrewd, very smart one. Though he restricts political liberty, he’s opened the markets; above all, he’s kept his own pockets clean. Everything there is so transparent; Singapore meets every requirement, every category, to become a global financial center. Its current account surplus is the highest in the region, almost 16% of GDP as of 1996. Singapore proves the point that whatever you do politically, you must respect the markets—though I think that eventually, free markets will lead to freedom.

China’s altogether different. First, China’s currency has zero convertibility, making its debt problems totally domestic. However, its 35% devaluation of the renminbi in 1995 hurt the export strength of the rest of Asia; and as other currencies fall, China faces pressure to devalue yet again, though no one expects it to do so. China’s export growth *is* expected to slow to 8% this year, from 20% last, but this shouldn’t hurt too much: at $120 billion, the country’s foreign debt is small; and at last count, it had $140 billion in foreign reserves. A projected growth rate of
over 6% for the next two years; a surging stock market in dollar terms; a tiny per capita labor cost that should protect it against regional devaluations—these are all sources of strength.

Yet danger lurks. Corruption is endemic—built into a system where prices are controlled but finances are not. Most of their nationally owned companies are hopelessly uncompetitive and poor. And worst of all, the Hong Kong Special Administrative Republic hasn’t turned out to be *quite* the dynamic money center the old Hong Kong was; the “red chip,” for instance, became one of the biggest frauds on the financial markets. Rapidly, investors are bypassing Hong Kong because of perceived Chinese interference; yet to the good, if this trend continues, it could spur further reform on the mainland.

Now, I *haven’t* much mentioned the country that’s the reason for the existence of this terrific Center—Japan. When I last spoke here—in November 1996, at the Center’s Tenth Anniversary Celebration—I detailed how bad things had gotten in Japan. Incredibly, due to the incompetence and arrogance of Japan’s bureaucracy, they’ve gotten *worse*. Stalled itself, Japan cannot lead Asia out of recession as the U.S. did Latin America, especially Mexico a couple of years ago. It’s not a matter of money—of which Japan still has plenty: as of 1997, a total private wealth of 1,200 trillion yen and an annual disposable income of 312 trillion yen—but a matter of will. Notes economist David Hale of Zurich Kemper Investments, “If Japan had provided Thailand with $10 billion rather than $4 billion, investors might have viewed Japan as a stronger regional leader capable of altering outcomes in several countries.” As Japan’s economy dwarfs all others, this is undoubtedly true. But Japan is so sunk in its own problems—though doing precious little to fix them—that it couldn’t care less what happens anywhere else. Just cleaning *itself* up would send salutary ripples throughout Asia.
At the latest G-7 meeting, Japan was roundly condemned. Unfairly or not, Japan was called a major cause of the Asian problem, and now an obstacle to the cure. After all, Japan pushed its development model throughout Asia, and was closely copied by at least Korea, Malaysia, and Thailand. And now, by doing nothing at home, it’s helping to shut down everyone else. If domestic demand and the currency were strong—the weak yen really started Korea’s problems—imports would gush in. If the banks had had adequate capital, they wouldn’t have tightened lending abroad as dramatically as they did. Unfortunately—as its 213% jump in the January trade surplus shows—it’s going to take the easy way out, resorting to exports, which is no solution at all to its fundamental problems. With its economy flat or shrinking, the banking system buried in bad debt—perhaps $700 billion worth—, you have to wonder, what are Japan’s leaders thinking? Are they thinking—at all? What sort of blindness keeps them on this barren path—a path that has put the country into nearly a decade of decay? I think that when the economic history of this century is written, one of the lead stories will be Japan’s mishandling its own economy. It’s a sad, demoralizing tale.

Their choices are dire. If, for instance, their banks are to meet the Basle capital requirements, they can do so by absorbing more equity, reducing total assets, or both—which they’re doing. They’re pumping 30 trillion yen into the system through junior convertible debt and other instruments, while reducing and focusing lending on their best customers. But there’s a cost here: being less risky, these customers are less profitable. If they’d learn sophisticated financial techniques—like risk management—they could take chances and win. In their management, they’ve got to learn to specialize, as we do in the West.

If Japan encouraged its own consumption and grew its economy by 3-5% a year, that alone could virtually solve the region’s problems. But it isn’t going to happen anytime soon—
thanks to the policy and management failures of the bureaucratic class. As long as you have a dominant group that’s interested only in maintaining its power, nothing good is going to happen to the country. In a way, the difference between Japan’s bureaucracy and a President Suharto is very small.

I know this is harsh stuff and I tell you, I wouldn’t bet against the Japanese were they to put the right policies in place. But worrying more about government spending, which constitutes 10% of the GNP, than about consumer spending, which takes up 60%, is just misguided.

You know, when you’re in Japan you don’t truly feel a recession. People look well, eat well, dress well; are constantly on their cellular phones. They don’t have a sense of panic, or even of discomfort. But productivity is down, as is trust in a system they once revered. The fastest growing industry in Japan now is private house safes—no one wants to put their money in banks. In the Third World, I could understand this, but in Japan!—this indicates a terribly serious problem, one that eats at the heart of society.

The bottom line of all this is that Asia must switch to a full market economy. The choice it has is, whether to make this switch somewhat painful, as it will be now, or very much more so if it waits—delays—resists. The saddest thing will be the suffering of the common people, who have far too little say in their affairs. Asia needs a new political class, one with a much higher level of sophistication and decency than it has now.

We may wish the markets away, but being rooted in the nature of our existence, they keep coming back. Fight them and you lose. The Anglo-Saxons are winning by working with the market. The lesson for Asia is: cooperate now, before it’s too late.

Thank you.