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East Asian Financial Integration: A Road
Ahead

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Abstract

ASEAN plus China, Japan and Korea have agreed to expand dramatically the scale of the Chiang Mai Initiative of bilateral swap arrangements and develop a more broadly focused institution. This could be a substantial step on the journey towards an Asian Monetary Fund ('AMF'). This paper examines what a fully fledged AMF would offer the region. The national economic policies of East Asian nations have differed substantially from those of the Washington Consensus, and been more effective. An AMF would offer the chance to promote economic policies in Asia that give a larger role to national government, equity investment and domestic demand, and a smaller role to foreign debt financing and export revenues, than do those of the Washington Consensus.

East Asian Financial Integration: A Road Ahead

by

Ross P Buckley*

ASEAN plus China, Japan and Korea have agreed to expand dramatically the scale of the Chiang Mai Initiative of bilateral swap arrangements and develop a more broadly focused institution. This could be a substantial step on the journey towards an Asian Monetary Fund ('AMF'). This paper examines what a fully fledged AMF would offer the region. The national economic policies of East Asian nations have differed substantially from those of the Washington Consensus, and been more effective. An AMF would offer the chance to promote economic policies in Asia that give a larger role to national government, equity investment and domestic demand, and a smaller role to foreign debt financing and export revenues, than do those of the Washington Consensus.

ASEAN comprises ten countries: Brunei, Cambodia, Indonesia, Malaysia, Laos, Myanmar, the Philippines, Singapore, Thailand and Viet Nam. Its people number some 570 million (McLean 2009: 20). Its combined GDP is only one-half as much again as Australia's, or about one-third of China's (Basic ASEAN Indicators June 2009). Yet it thinks big. The grouping aims to become a European Union style economic community without the common currency by 2015 (ASEAN 2007).

This, to me, is empty rhetoric. European union was underpinned by the need to combat profound security threats that had ravaged Europe twice last century, and for much of the

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preceding centuries. The security imperative that drove union in Europe is not present in East Asia, the decades of groundwork that paved the way for union in Europe have not been undertaken in East Asia and, as an idea, East Asian union does not appear to have anything like the profile or support that European union had even 20 years before it came to pass, let alone in the handful of years remaining until 2015.

Indeed I wonder whether the concept of 'Asia' today is as strong as the concept of 'Europe' was 30 or 40 years ago. The core European countries were bound by a common religion, and a long history of fluid borders. China's borders are essentially similar today to what they were 2,000 years ago. The Vietnamese see their history as a separate people stretching back 4,000 years. 'Asia' today is perhaps a concept used more often by those outside the region seeking to define or constrain it, than by those within the region seeking to understand it.

So, for what it is worth, I think political union is a long way off. However, closer economic and financial integration is a different matter. Closer economic integration is proceeding apace. Closer financial integration is realisable and much needed; and may also, eventually, serve as part of the groundwork for political union.

Closer financial integration is realisable because East Asia has the world's largest foreign exchange reserves, highest savings rates and most dynamic economies.

Closer financial integration is much needed because the Washington Consensus policies promulgated by the International Monetary Fund ('IMF') and World Bank have been a conspicuous failure in promoting development, and just when the need for economic growth is at its highest in the aftermath of the global financial crisis, there is a vacuum in the International Financial Institutions as to the policy settings likely to promote it. Such integration is also desperately needed because over the past two decades, 'capital-account crises have been the norm rather than the exception' (Bird and Rajan 2006: 336). Its massive savings as a region gives East Asia more options in dealing with global capital than do most regions, and provide the opportunity to interact with global capital more on its own terms.



A virtuous cycle is potentially achievable here. Greater regional integration of financial systems through an Asian Monetary Fund should lead to greater regional stability; which should lead to more of these savings, both individual and sovereign, staying in Asia; which should, in turn, lead to even more regional stability. The great paradox of the East Asian crisis of 1997 was that it was brought on by foreign capital losing confidence in a region with the world's highest savings rates. If East Asia could have kept its money at home, it never would have needed foreign capital, and there would have been no chance of a crisis provoked by an exodus of foreign capital.

The region, especially with China's rise as 'factory for the world', has seen increasing levels of trade and economic integration. Many manufacturing processes today are centered in China but combine inputs from throughout the region in a hub and spoke system in which other nations contribute in their areas of comparative advantage to the Chinese production.

Trade integration has continued apace. ASEAN and China entered into a Framework Agreement on Comprehensive Economic Cooperation in 2002 and another agreement on trade in goods in 2004. Under these agreements a free trade area will come into effect between China and ASEAN's five founding members and Brunei in 2010, and be extended to embrace ASEAN's other four members in 2015. In February 2009 ASEAN entered into a free trade agreement with Australia and New Zealand covering trade in goods, services, e-commerce, the movement of persons and investment.

The region is developing a 'noodle bowl' of regional and bilateral trade agreements. For instance, in the case of Australia as well as the agreement with ASEAN and New Zealand considered above, there are bilateral agreements with Thailand, New Zealand and Singapore and ongoing negotiations for over four years and 13 rounds on a proposed Australia-China FTA and for two years and eight rounds on a proposed Australia-Japan FTA. In the interests of trade, and especially administrative, efficiency one can but hope that one day this noodle bowl of different agreements will be replaced by one free trade area extending from New Zealand to China and South Korea to Australia and embracing all the nations within the East Asian region (and perhaps even India) (Asian Development Bank 2008).



However, the financial integration of the region has lagged far behind its economic and trade integration. In the words of an IMF study,

intraregional financial integration – for example measured directly by cross-border capital flows or indirectly by cross-border correlation of consumption growth – has been more limited than elsewhere. Consequently, Asian economies appear to have become more integrated with countries outside the region than within the region. (Cowen and Salgado 2006: 4)

The seminal event, in terms of East Asian financial integration, was the East Asian financial crisis of 1997–1998. It had two immediate consequences. First, because no Asian organisation was able to provide support to any Asian state it led ‘to the irony that Indonesia, South Korea and Thailand faced an invasiveness towards national policymaking, especially through credit conditions, that was contrary to all ASEAN precepts’ (Arner, Lejot, Wang 2009: 13). This experience caused financial cooperation to replace trade cooperation as the number one regional priority. To this day, the changes to domestic policies which the IMF forced upon countries as the price of the bail-outs, and the profound extent to which the IMF initially misdiagnosed the causes of the crisis, are deeply resented throughout the region.

Secondly, it brought into being the ASEAN + 3 grouping, comprised of the ten ASEAN nations plus China, Japan and Korea. ASEAN + 3 had its first summit in Kuala Lumpur in December 1997. In a short time frame, ASEAN + 3 supplanted APEC as the principal economic organisation within the region (Arner, Lejot, and Wang 2009: 23). Since then ASEAN + 6 (which includes Australia, India and New Zealand) has been developed, in part at the urging of smaller states seeking counterweights to the potential influence of China, and to a lesser extent, Japan (Arner, Lejot, and Wang 2009: 16).

In the immediate aftermath of the East Asian crisis in 1997 Japan offered to fund the establishment of an Asian Monetary Fund, but the idea met stern opposition from the United States (‘US’) and the IMF, and a lack of support from China, and was dropped (Lipsev 2003). In its place, the much less ambitious Chiang Mai Initiative was pursued, a series of bilateral commitments by which regional nations committed to make bilateral



swap arrangements and security repurchase agreements available to each other in times of need.

Over time the size of the bilateral swap arrangements were steadily expanded, while the potentially useful repo arrangements were ignored and never really used. This slow trend received a huge boost in February 2009 when the swap agreements were multilateralised and increased by US\$40 billion to US\$120 billion in an agreement among ASEAN+3 finance ministers known as the Multilateralised Chiang Mai Initiative ('MCMI'). China, Japan and Korea are to provide 80% of these commitments, with the balance to come from ASEAN nations. Recent research suggests that the pre-2008 bilateral swap agreements were used in broadly efficient ways (Kohlscheen and Taylor 2008: 330). The MCMI should be far more efficient and effective, because the commitments will be multilateral.

Under the MCMI, Indonesia would be able to draw, as of right, about five times as much as under their official IMF reserve tranches (although in practice the IMF often exceeds these official levels of lending) and the Philippines six times as much as the official IMF commitments (Kohlscheen and Taylor 2008: 324).

With the implementation of the MCMI in March 2010, for the first time, regional nations will have what they needed in late 1997: a credible alternative to the credit lines extended by the IMF. However, the MCMI credit lines are not genuine alternatives, because 80% of the amounts available for drawing thereunder are not available unless a nation has an IMF program in place. In this case therefore, even if the MCMI had been in place in 1997, 80% of the funds could not have been disbursed when most needed, in a timely fashion, as IMF negotiations dragged on for months.

The apparent reason for conditioning MCMI credit upon an IMF program is that to date the CMI has not had any real surveillance capacity. The commitments made in February, 2009 address this issue: 'An independent regional surveillance unit will be established to promote objective economic monitoring' (Finance Ministers of ASEAN + 3 2009).

It is easy to be optimistic about the MCMI. Yet it is today nothing more than a series of commitments, by an organisation, ASEAN, which doesn't have a strong record of turning commitments into concrete achievements. While the MCMI has come into effect, concrete commitments are yet to be made, with the credit and reserve pooling commitments still to be agreed. (Lejot, 2010) The temptation to excessive optimism is large, because the MCMI is so needed, and the institution to which it would logically be the precursor, so important. For a series of substantial credit lines coupled to a serious surveillance (and thus advice-giving) capacity is very close to a monetary fund, in this case, an Asian Monetary Fund. And it is the prospect of an Asian Monetary Fund that excites the imagination of those who care about the region, and its potential to chart its own economic course and contribute to global prosperity.

So the first step is to temper our optimism and recognise that the realisation of the MCMI commitments is, given ASEAN's track record, likely to take some years. Its success will require a willingness to either share sovereignty or to allow one state to design and lead the initiative (Arner, Lejot and Wang 2009: 49), and there is precious little in the history of ASEAN, in the over four decades since its inception, to suggest either of these paths will be anything but difficult.

Still these are sound reasons to explore, analyse and invest intellectual capital into the idea of an Asian Monetary Fund, not to dismiss it as unlikely to come to pass.

AN ASIAN MONETARY FUND

The nations of East Asia have enjoyed decades of extraordinary and sustained growth. For over 20 years China has grown at an average rate above 9%, Malaysia, Singapore and South Korea have all grown at annual average rates above 6%, and Taiwan and Thailand at 5.5% and 5.9% respectively (Ghosh 2005; CIA Factbook 2009; Economist Intelligence Unit 1993 and 1995). When Japan was outperforming the world, from 1950 to 1965, its economy expanded on average at over 10.4% per annum (Beida 1970: 12).

China is today the second largest economy in the world in purchasing power parity ('PPP') terms, the terms that economists generally accept are best used for comparative



purposes, and the third largest economy in unadjusted US dollar terms (Seager 2010). China's GDP on a PPP basis in 2008 was \$7,916 billion and its per capita GDP on the same PPP terms was \$5,963. This compares to \$14,625 billion and \$46,859 for the US (International Monetary Fund 2009).

If the same policies had worked in each of these East Asian nations and differed from those of the Washington Consensus we would have a neat, simple story. But real life is rarely neat. As HL Mencken wrote, "There is always an easy solution to every human problem – neat, plausible and wrong" (*New York Evening Mail* 1917). Indeed, the inherent and deeply embedded diversity of nations is part of the problem with the Washington Consensus – its one-size-fits-all mindset, in truth fits very few countries.

The policies that have delivered success to different East Asian nations over time have varied, considerably, from each other but one of the commonalities has been a much larger role for government in most of these countries than is permitted under the Washington Consensus. Certainly Japan has consistently preferred regulatory approaches "that rein in rather than let loose market forces" (Lipsey, 100). Indeed, the only East Asian country to consistently follow Washington Consensus policies fairly closely has been Hong Kong (treating it as a separate economy for these purposes).

China has followed the classic development path of moving from an agriculture-based economy into manufacturing, initially simple manufacturing such as clothing and footwear, and then ever more sophisticated manufacturing, to the point that today China is the 'factory for the world', the way the North of England was in the early years of the industrial revolution. The 'final' stage on this classic path, followed by developed countries, is the further transition into a services-based economy.

For most of the past 25 years China has been a command economy. Even today China is perhaps best described as a soft authoritarian system. Certainly it is a very different political system to the democracies of most East Asian nations. For an example of the role of the state in China's economy consider that, as recently as 2004, state-owned enterprises accounted for over 50% of China's GDP and over 40% of its exports (Ghosh 2005).

These different paths and systems have been supported and reinforced by the differences between the financial systems in each country. China has retained state control of its financial sector and has used this control to manage the economic cycle and to direct funds to priority sectors of the economy, precisely as it is doing today to combat the Global Financial Crisis ('GFC'). Most other East Asian nations have relatively low levels of state ownership generally and of their financial sector in particular (Ghosh 2005). Accordingly, their financial sectors have not provided government with a tiller with which to direct, and control, the economy as has China's.

China has invested significantly in education of late, and is increasing this investment rapidly. According to Premier Wen Jiabao's state-of-the-nation address in March, 2008, the central Chinese government quadrupled health spending in 2007 and lifted spending on education by 76%. The Premier promised to lift health spending a further 25% and education spending a further 45% in the next year, and also promised steep increases in social welfare spending. These expenditure increases were underpinned by sharp increases in government revenues, up nearly 35% in 2007 (Garnaut 2008: 9). The GFC has since curtailed these revenue gains, but the direction is clear.

These funding increases in China come atop a solid base: 74% of young people of school age were in school in China in 2005 (World Bank 2009). Furthermore in China girls are as likely to be in school as boys, which is reflected in literacy rates. In China 99% of young women between 15 and 24 are literate.

Education is critical for growth. China's investment in education means that its deep pool of workers have been able to make the transition into manufacturing jobs because their education has enabled the transition. This large workforce is able to supply labour to manufacturing industry, and equipped to do so by massive state investment in education — not a condition for development repeated in many developing states (He 2005: 195).

There are few investments that generate as strong returns for a developing nation as investing in the health and education of their children (Lustig 1998; Lustig 2000).

China's current spending priorities suggests it understands this, deeply. As Susan George wrote 20 years ago, 'The IMF cannot seem to understand that investing in ... [a] healthy,

well-fed, literate population ... is the most intelligent economic choice a country can make' (George 1990: 143, 187, 235). Recent IMF and World Bank practice suggests the IFIs are still to learn this lesson (Buckley 2009).

THE WASHINGTON CONSENSUS POLICIES

The focus of the Washington Consensus policies has been to grow the debtor's economy, so as to alleviate poverty within the country and generate sufficient foreign exchange resources to service its debts. It has been taken as axiomatic that higher growth rates lead to less poverty, that higher growth rates are only possible once economic stabilisation has been achieved, and that higher growth is best achieved on the back of exports, not increases in domestic demand. The policies imposed to achieve these goals typically included:

- reductions in the budget deficit to limit inflation, and the need for foreign borrowing,
- limits on domestic credit expansion to control inflation,
- exchange rate devaluations to discourage imports and encourage exports,
- liberalisation of tariff and quota regimes, and
- a much reduced role for government and a much increased role for markets.

Other Washington Consensus policies imposed on debtors, at times, included (i) higher income and sales taxes, (ii) higher charges for state-produced goods and services such as electricity and water, (iii) privatisation of state-owned companies, and (iv) deregulation of the labour market. These policies have been criticised for their adverse effect on economic growth and their devastating effect upon the living standard of the local people, particularly the poor (Bello 1994; Green 1995; Beeson and Islam 2005; Dosi, Imoli, Stiglitz 2009).

The Washington Consensus has encouraged export-led growth for developing countries (Palley 1999). However, a reliance on exports exposes developing countries to the vagaries of demand in developed and other developing countries and to the extreme volatility of global commodity prices. A better policy admits of a larger role for domestic demand-led growth. In Palley's words, '[t]his is a strategy that lifts all boats since

demand growth in one country pulls in exports from others, so that all grow together' (Palley 1999). The final word on the Washington Consensus goes to Professor Hal Scott, 'there is little evidence that IMF conditions, usually requiring contractionary fiscal and monetary policies, have worked' (Scott 2003: 115).

To understand how the IMF came to have, as its primary role, the direction of the economies of debtor nations in crisis and the implementation, therefore, of the Washington Consensus, it is necessary to understand its history.

A BRIEF HISTORY OF THE IMF

The IMF was founded, along with the World Bank, in 1945 to, in the words of its website,

promote international monetary cooperation, exchange stability, and orderly exchange arrangements; to foster economic growth and high levels of employment; and to provide temporary financial assistance to countries to help ease balance of payments adjustment.

This is a reasonable summary. But the website proceeds,

Since the IMF was established its purposes have remained unchanged but its operations—which involve surveillance, financial assistance, and technical assistance—have developed to meet the changing needs of its member countries in an evolving world economy.

At best, this is spin, for the Fund's purposes have changed. They changed in the 1970s when most developed countries moved away from fixed, to floating, exchange rates and the core function of the Fund, the maintenance of exchange stability, was ceded by governments to the market.

The Fund performed a useful function throughout the 1950s and 60s, which were periods of sustained growth in much of the world, but by the end of the 1970's the Fund had a much reduced mission. This all changed with the debt crisis of 1982. The crisis gave the Fund the chance to reinvent itself as the manager of developing country crises. Debtors needed new money, to at least service interest. Creditors wanted assurances that the debtor's economic policies that had contributed to the crisis had been changed, and had firm views on the need for economic austerity by countries whose debt they were

rescheduling. Yet direct commercial bank involvement in the setting of local economic policies was a political impossibility. The IMF was ideally placed, as an apparently independent international financial institution, to determine and monitor the economic policies, going forward, of the debtor nations.

These policies imposed by the IMF and the World Bank, and supported by the US Treasury, came to be known as the Washington Consensus as all three bodies are headquartered in Washington, D.C. Yet these policies flew in the face of the experience of OECD countries. Britain in the nineteenth century, and the United States in the twentieth century, promoted free-trade 'because they were the most efficient producers of the highest value-added goods. They did not become so through free trade; they protected themselves for decades in order to achieve that end' (Castaneda 1993: 464).

THE DEBT CRISIS OF 1982

In the early years of the debt crisis the Fund severely underestimated its magnitude and responded with ineffective policies. IMF policy prescriptions for Africa and Latin America meant the 1980s were a lost decade, in which net capital flows were northbound, in which infrastructure crumbled, and in which life expectancy at decade's end in Sub-Saharan Africa was shorter than at the beginning (Bos 2006: 12).

The debt crisis was relieved for the banks by the Brady Restructurings of the early 1990s in which the loans were converted into tradable bonds at a discount, with security for the repayment of principal and some interest. The Brady process did less for the debtor nations than the banks but brought some modest relief and encouraged new capital inflows. Of importance for this analysis is that the Brady Plan was devised initially in Sao Paulo and Mexico City and then given the imprimatur and support of the US Treasury (Buckley 2004). The IMF had no substantive input into crafting the only creative measure brought to bear on the debt crisis.

THE ASIAN CRISIS OF 1997

Asia's was a fundamentally different crisis from the debt crisis of 1982 or Mexico's peso crisis of 1994–95 in that the great majority of the troublesome indebtedness was of the

private, not the public or quasi-public, sector and it was not a crisis of over-consumption. Latin American nations had borrowed to fund government budgets. East Asian governments had not been similarly seduced. In the words of Laurence Meyer, a Governor of the US Federal Reserve System,

By conventional standards, the monetary and fiscal policies of the developing Asian economies prior to the crisis were largely disciplined and appropriate. ... consumer price inflation ... was relatively subdued [and] fiscal policy also appears to have been disciplined. (Meyer 1999: 5)

Asia's crisis was primarily a crisis of inadequate local prudential regulation and inadequate confidence of global capital in the region (Buckley 2000). It was a contractionary crisis. Notwithstanding all of these differences, the IMF waded into Asia imposing the Washington Consensus policies it believed had worked in Latin America in the 1980s and Mexico in 1995 – prescriptions of budgetary tightening and austerity. Austerity is always bad policy for a contractionary crisis. It is utterly ineffective in encouraging contracting economies to expand. At the time the Nobel laureate, Joseph Stiglitz, was the Chief Economist of the World Bank and he spoke out repeatedly to highlight the fundamental error in the Fund's response to the Asian crisis (Passell 1998: D2, Col 1). Joe Stiglitz was to be proven right, but when it mattered most, the IMF wouldn't listen to him.

The IMF eventually acquiesced to requests by national governments for more expansionary policy settings but by then considerable, unnecessary economic damage and human suffering had occurred. Furthermore, the Fund only eased its austerity policies. In the meantime, Malaysia had adopted more successful strategies that remain outside the Fund's kitbag of policy options (Buckley and Fitzgerald 2004: 96).

Malaysia refused IMF funding and advice and chose to chart its own way out of the Asian crisis, imposing capital outflow controls to keep foreign capital within the country, and pegging the ringgit to the US dollar (Buckley and Fitzgerald 2004). Malaysia was then able to ease monetary policy and pursue expansionary fiscal policies, without being hampered by concerns about the impact of capital outflows on exchange and interest rates.



Malaysia had created as close to a controlled laboratory experiment as one gets in economics. Thailand and Korea sought to exit the crisis using the Fund's policies. Malaysia followed a different course. (Indonesia is a separate case, as its high debt levels meant it was in a different type of crisis). All three economies recovered, but Malaysia's recovery was more rapid, and its poor were harmed far less (Buckley and Fitzgerald 2004). As Kaplan and Rodrik put it, 'compared to IMF programs, ... Malaysian policies provided faster economic recovery... smaller declines in employment and real wages, and more rapid turn around in the stock market' (Kaplan and Rodrik 2004).

Yet the Fund's mistakes in East Asia, so clearly highlighted by Malaysia's taking the road less traveled, paled in comparison to its egregious errors in Argentina.

ARGENTINA'S IMPLOSION IN 2001

From 1991 to 1998 Argentina prospered as its GDP per capita increased 44% and inflation was under control (Kiguel 2004: 84). Argentina improved its banking system, more than doubled its exports, privatised a broad range of industries, experienced significant growth in oil and mineral production and achieved record levels of agricultural and industrial output (Kiguel 2004: 101–1). It was the darling of the IMF and global financial markets and toasted as 'the best case of responsible leadership in the developing world' (*The Nation* 2002: 3).

Nonetheless in late 1998 Argentina entered a severe recession caused by excessive borrowing to support general government expenditure, the peg of the peso to the US dollar, and Argentina's endemic corruption (Buckley 2003: 373). The recession was magnified by massive capital flight, so that the government had to impose harsh caps on withdrawals from bank accounts, and eventually close the banks. Still the crisis deepened when the IMF refused to extend further credit to the nation in 2001, believing its economic programs to be unsustainable. As commercial lenders followed this lead, Argentina was forced to default on its external debt of some US\$132 billion.

Argentina was exceptionally resolute in its negotiations with its external creditors and refused to accept conventional levels of debt relief. President Kirchner refused to service



the debt from the 'suffering and hunger of the people'. He had good grounds: Argentina's poverty rate, 27% in 1999, by 2003 had doubled to 54.7%; per capita GDP, US\$7,800 in 1999, by 2004 had fallen to \$3,800; and debt that represented 47.4% of GDP in 1999, by 2004 was 140% of GDP (Hornbeck 2004: 4).

In early 2005, 76% of Argentina's creditors accepted its offer to exchange its debt for bonds at the unprecedented discount of some 66 per cent on a net present value basis. Argentina emerged from its default on the most advantageous terms ever secured by a middle-income country in a debt restructuring. In the words of *The Financial Times*, 'Argentina gambled, and the gamble paid off' (*Financial Times* 2005: 20).

In contrast, the IMF emerged with its credibility in tatters. Never before had a country that had so faithfully followed the Fund's policies collapsed so severely, never before had the Fund's image been so badly damaged by a sovereign default.

AN ASIAN CONSENSUS

Other nations should be grateful that China and the other nations of East Asia have ignored IMF advice, and take their own paths, because for decades the stellar economic growth of East Asia has lifted that of the world. China's capacity to produce manufactured goods, clothing and other items ever more efficiently and cheaply has kept a lid on inflationary pressures in virtually all developed economies. For Australia, Brazil and other commodities exporters China's growth has provided a massive market for minerals and other commodities. Indeed, the rise of East Asia generally underpinned global prosperity in the two decades leading up to the global financial crisis.

East Asia is uniquely placed in terms of domestic savings rates and foreign exchange reserves. China and Japan hold nearly 20% each of worldwide official foreign currency reserves (Kohlscheen and Taylor 2008: 323). For many years, China and Japan have been the principal buyers of US Treasury bonds. The Chinese and Japanese have saved and lent, so Americans can borrow and spend.

China has amassed massive foreign exchange reserves, on the back of a most probably undervalued currency. These reserves serve as splendid insurance against global financial

instability. Recent research suggests that while China may well be manipulating the value of its currency, it is not in breach of its obligations under the Articles of Agreement of the IMF or the various WTO treaties (Mercurio and Leung 2009). A nation cannot maintain an under-value for its currency and control its interest rates if it needs global capital (Obstfeld and Rogoff 1995; Obstfeld, Shambaugh and Taylor 2005). It is only the independence that high domestic savings rates give a nation which allow the long-term manipulation of the value of its currency. China has started to allow the yuan to appreciate. It announced on June 19, 2010 that the 23 month freeze on the yuan against the US dollar would be relaxed and gradual change in the value of the yuan would be allowed within a daily trading band of 0.5% (Rich 2010).

The success of Asia, East and South, highlights the weaknesses of the Washington Consensus policies. China and India are two very different nations, with different political systems, development paths, financial systems, and economic policy settings. Yet both nations have far outperformed those implementing Washington Consensus policies. It is arguable that China and India have unique advantages not available to other developing nations. China's advantages include a massive supply of relatively well educated, cheap labour and a huge potential domestic market which China has used adroitly to lure inbound FDI (and ensure high technology comes along with it). India's advantages include a similarly large, cheap workforce coupled to the widespread facility with the English language, the English common law legal system and other institutions, and its tradition of excellence in mathematical and scientific education.

So comparisons between China or India on the one hand with other developing countries on the other may not be fair or informative. However, comparisons between China and India suggests the policies of the Washington Consensus are misguided. For of the two nations, India's policies are closer to those of the Washington Consensus than China's. Government has a much smaller role in the Indian economy than in China's. The market is the major allocator of financial and other resources in India, much less so in China. Yet China has consistently outperformed India, and, given the increased investment in its human capital which China's economic growth has made possible, it is likely to continue to outperform India in the foreseeable future.

CONCLUSION

For years Western experts have been predicting that China's high growth rates could not be sustained (Kreuger 2008; Gailbratih 2000; Prassard 2004; Dekle 2005). The weakness of its institutions, such as the rule of law and independent courts, mitigate against sustained growth in Western eyes. But China's continued growth, far beyond the limits the experts were certain would constrain it, suggests that China may have crafted its own paradigm in which the lessons of institutional economics need to be revised. Whether that system is transferable to other nations, with different work ethics and cultures and levels of entrepreneurship is another matter. What is clear is that Washington Consensus policies have not worked in most countries to which they have been applied, and the policies that engendered such dramatic and sustained periods of growth in China, Japan, South Korea, Singapore, Malaysia, Taiwan and other countries are quite different to those of the Washington Consensus.

An Asian Consensus would, logically, be an amalgam of the policies that have worked to empower East Asian economic growth and lift massive portions of the region's population out of poverty: policies that allow a larger role for government, that prioritise inbound equity investments over debt and focus on investments that bring with them high technology and management expertise, and policies that emphasise nation building through investment in the education and health of the local people rather than the repayment of foreign debt.

An Asian Monetary Fund could develop and promulgate this Asian Consensus and thereby pioneer new approaches to the development challenge. It could serve the region far more effectively than the International Monetary Fund and its Washington Consensus policies ever have.

The second reason an AMF represents a great opportunity is that presently the region is not benefiting, as a region, as much as it could from its massive foreign exchange reserves. An Asian Monetary Fund could work to more fully develop regional bond markets and take other initiatives to keep the region's savings in the region. Greater regional financial self-sufficiency



would serve to insulate the region from the volatility that comes with a dependence upon foreign capital.

A decade ago, Eichengreen and Bayoumi concluded about East Asia that ‘there is little sign, comparable to the evidence which has existed in Europe for nearly 50 years, of a willingness to subordinate national prerogatives to some larger regional entity’ (Eichengreen and Bayoumi 1999: 11). A decade later this is less true than it was, but is still not wrong.

So the road to an Asian Monetary Fund will likely be long, and difficult. But the first major steps have been taken. An AMF represents the chance to move away from a development model that is focused primarily upon ensuring poorer nations are able to service their debts and move towards a model that is genuinely focused upon the development of the nations themselves and their people. An AMF also represents the chance to use the region’s foreign exchange reserves to insulate the region against the destabilizing effects of global capital and the capital account crises that currently accompany globalised international finance. The people of East Asia deserve nothing less.

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