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'Need for a regional mechanism'

By HARDEV KAUR

The biggest challenge for Japan and South-East Asia is to really create some kind of regional mechanism to grow together. In a wide-ranging interview with HARDEV KAUR, Dr Eisuke Sakakibara, former Japanese Vice-Minister of Finance and International Affairs, says the region must be vigilant to face the present uncertainties.

QUESTION: The Japanese economy is picking up but there is also a problem with the higher oil prices. Can Japan still act as the engine of growth for the region?

ANSWER: There are a lot of uncertainties. One is oil prices, but the Chinese economy seems to be quite a problem. A soft landing or a hard landing - it will probably take place within the next year or so, and inflation is picking up in China and elsewhere. Although the Japanese manufacturing sector has recovered, there are lots of uncertainties ahead. The US economy is probably at its peak now. It will start to come down. So this is what I call a paradigm shift from deflation or disinflation to inflation. From easy management policies to heightened management policies in all countries and this paradigm shift will certainly affect the Japanese economy. If the current conditions continue, the Japanese economy could grow at a little bit over 3 per cent. It has recovered and probably the figures from January to March and April to June will be quite good. But what happens after summer really depends on a lot of factors - oil prices and shift of monetary policy in the US and in China, and elsewhere.

Q: What does this mean for South-East Asian countries, especially Malaysia, Indonesia, Thailand?

A: We need to be vigilant. Not only Japan and South-East Asian countries. China's economy is probably at the peak and has some bubbles, and the bursting of the Chinese bubble will have a major impact not only on Japan but on the South-East Asian countries as well, because our economies, at least in terms of the markets, are quite integrated. China is one of the biggest factors in the region at this moment.

Q: The announcement by the Chinese authorities that they will perhaps look for a soft landing. Will that work?

A: Half and half. Some Chinese policymakers, particularly the People's Bank of China, are very much worried about their stocks and they want to tighten the monetary policy. There are other economists in the Government who think that overheating is quite partial, so Chinese authorities do not have to worry about it. It looks like the Government is somewhat split. So further effective tight monetary policies could be implemented in the short period of time. If they could, they may be able to have a soft landing. If they don't, it would be hard landing. So it's quite crucial.

Q: This is happening when the economy is just beginning to pick up and is likely to impact the region's economy. You had suggested the setting up of the Asian Monetary Fund during the financial crisis. Is there a need for the region to get together to look after itself?

A: I think so. The region has huge amounts of foreign reserves. Japan and China together have a little over US\$1.2 trillion (US\$1 = RM3.80) in foreign reserves. If we could have about 2 per cent of them that would be a sufficient amount to set up something like the Asian Monetary Fund. I think we should do that because we may. I'm not predicting it, but we may

encounter another (financial) crisis and we need to be vigilant.

Q: Prime Minister Datuk Seri Abdullah Ahmad Badawi suggested that if the full-fledged Asian Monetary Fund is not possible at this time, perhaps we need to consider a think-tank as a precursor to the proposed monetary fund. Do you think that would be feasible or that the Asian Monetary Fund will be acceptable at this point in time?

A: That's one way to go, to have the think-tanks to coordinate. That is the initial stage for a full-fledged Asian Monetary Fund. If the governments agree to pool 10 per cent of their foreign reserves to be used for various regional policies including crisis preventive measures, that would do it. We should have a full secretariat for the kind of mechanisms we need, that could be discussed. The important thing is to pool part of the reserves and to jointly manage that fund. It would be difficult but the region has such huge foreign reserves. Why not do it?

Q: We already have the Chiangmai Initiative. Do you think it should be taken forward towards the eventual establishment of the Asian Monetary Fund?

A: Yes. The Chiangmai Initiative could be expanded. It is a network of bilateral relationship. So we could accept some sort of multilateral mechanism to pool the resources.

Q: Can the Japanese economy be depended on to pull the rest of Asia along with it?

A: No. If China collapses, it will be difficult for Japan to become the engine. Japan and China, to some extent, are fairly inter-dependent. The Japanese economy is significantly dependent on China and the world economies are truly internationalised.

Q: There are numerous calls by the US, and to a certain extent Europe, for China to revalue the yuan. Is it a good thing?

A: No. Not at this time. China is now running a trade deficit. Why should a country running a trade deficit appreciate its currency? That doesn't make sense.

Q: During the financial crisis, they did not devalue the currency. Do you think they will also not do so now as it could set out another round of problems?

A: Yes. I meet with the Chinese authorities quite regularly and they have said consistently that they will not at this moment devalue the currency. Of course, they will eventually adjust the mechanism and deal with capital controls but there will be some sort of a time span of five to 10 years.

Q: What is the biggest challenge for Japan and South-East Asia?

A: The biggest challenge for us is to really create some kind of regional mechanism to grow together and to defend ourselves against negative external factors. Markets are moving in that direction. Private sectors and market forces are now being integrated very quickly within the region and the authorities need to follow the market.

Q: The European Union is integrated starting with trade. But as you pointed out the markets are already integrated. Should Asian countries follow Europe and go for trade integration because we are already integrated in a lot of ways?

A: We should proceed on all fronts - one Chinese economist calls it PPP - Partial Parallel Progression. We should push it on all fronts simultaneously.

Q: With US elections this year there seems to be a standstill as the American focus is somewhere else. Should Asia take the lead. Will Asia take the lead?

A: We should. We should coordinate our moves. The US has gone into a quagmire with regards to Iraq and they can't move. The Iraqi and West

Asian situations are getting worse and worse. It will get even worse. This is having a negative impact on oil prices, and oil prices in turn have an impact on world recovery. The situation is deteriorating. The world economy is recovering, but it is probably at the peak now and we will probably start to decline from the summer of this year due to various disruptions. We, therefore, need to set up some sort of regional mechanism to defend ourselves.

Q: Japan, which is heavily dependent on oil, probably will have the biggest impact on the region.

A: Yes, Japan will have, but China right now has become the main importer of oil as well. Indonesia might be very rich for it, Malaysia, too will benefit (as a producer). Big consumers like Japan and China will really suffer.

Q: Do you think the US Federal Reserve chairman Alan Greenspan will raise interest rates?

A: The market expectation is that he will raise the interest rate by 25 basis points at the next Federal Open Market Committee meeting which is scheduled for the end of this month.

Q: Would that be a good thing especially at this time?

A: I think that he has to do it. If he doesn't, it would be a major surprise to the market and Greenspan usually does not surprise the market.

Q: The world trade talks, under the auspices of the WTO (World Trade Organisation), are not going anywhere. What should the region do? There are a lot of moves to bilateral and regional cooperations. Will that help?

A: Tun Dr Mahathir Mohamad made a speech at the Keio University and he was referring to the Free Trade Agreement (FTA) with Asean (the Association of South-East Asian Nations) countries. Japan should negotiate an FTA with Asean. China is negotiating an FTA with Asean. So Japan should follow China in negotiating an FTA with Asean countries as a group rather than going ahead on a bilateral basis. But that initiative at this moment is not being taken in Japan, I am sorry.

Q: But why? Why is Japan so reluctant?

A: I don't know. They are just proceeding on a bilateral formula.

Q: Could it be because with a bilateral agreement, such as that with Singapore, it is much easier to negotiate because the conflict areas and agriculture, do not feature in the negotiations?

A: Yes, but they are now negotiating with Thailand and South Korea. It is difficult but I've been dealing with the Japanese agriculture sector which seems to be undergoing some major transformation so that within a matter of the next two to three years an FTA including agriculture will become feasible. And we really need to do that (negotiate an FTA). There are some moves here and I'm trying to promote that.

Q: The Japanese banking and financial system ... is it healthy enough now?

A: It's much healthier than say two or three years ago and I don't see any major crises in the coming years. We still have a problem with regards to the local finance. Major city banks have been consolidated and have improved their balance sheets. But there are some local banks which have not made much progress so far. So we still have some problems but some improvements have been made.

Q: So in your opinion, the outlook for the world economy isn't very good now?

A: The world economy seems to have recovered, but now the recovery is about to end, unfortunately. Because of various bottlenecks - the bottlenecks being Chinese bottlenecks in electricity and the energy sector.

Q: The rise of Asia is still being hampered to a certain extent?

A: Yes, but we need to cooperate with each other at the time of the slow down, at the time of the crisis.

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