

**THE INTERNATIONAL CONFERENCE ON MANAGING THE ASIAN
FINANCIAL CRISIS: LESSONS AND CHALLENGES**
PALACE OF THE GOLDEN HORSES, SG BESI, 2 NOVEMBER 1998

Dismissed initially as an Asian problem when it began last July, the East Asian financial crisis has now ballooned into an economic upheaval of global proportion. The financial crisis has since spread to Russia -- where the IMF has again failed to rescue. More recently, the financial shockwaves have reached the American shores. Several Latin American countries, facing massive capital outflows and currency devaluations, may need to resort to the IMF soon. With the contagion now spread across three continents, the threat of a global recession looms large. What went wrong? Is something amiss or different about this crisis? Or is it just the scale and the speed? Has technology advanced beyond human control? To know this we have to know the root causes and the secondary and even tertiary causes if there are any.

2. We have to remember that the East Asian countries prior to their financial collapse were among the most successful economies in the world. The economic success is real although attributing it to miracles was quite wrong. These countries grew fast economically because they had apparently found the formula for growth. The formula is not the same but certain elements were common.

3. South Korea was ultra-nationalistic. It did not want foreign companies to invest and develop its industries. It preferred buying technologies and breeding its own entrepreneurs and industrialists. Japan was its model and a source of its technologies. Koreans with any potential at all were given protection and funds by the Government to go into practically any industry they chose to. Those who succeeded would get even more help. Very quickly huge counterparts of the Japanese trading houses emerged.

4. Although these chaebols were largely privately owned, it did not prevent them from contributing tremendously to the rapid development and industrialisation of Korea. They may be considered as cronies of the Government but the cronyism came mostly after the Government recognised their potential to succeed and to help propel the country's industrialisation. Besides, their success brought employment for the Korean workforce and helped the small and medium industries. It would be wrong to say that nobody except themselves gained from their success. It is also doubtful if public limited companies were floated in order to venture into the unknown territory of the large-scale industries, such public limited companies would succeed. Certainly rapid success would not have been possible as the management and decision making process of public companies are complex, tedious and cautious. Companies with strong leadership by the proprietor chief executive are much more able to make forays into unknown territories and to take bold actions to overcome obstacles.

5. Obviously any lack of skill would result in early failure and dropping out. So a few would survive and succeed. And these would grow very rapidly, especially as the Government with nationalist objectives extending helping hands.

6. Within a very short space of time a number of chaebols emerged which seem capable of unlimited growth in every direction.
7. Rapid growth necessitates borrowing huge funds, first from domestic sources and then from foreign sources. Cash-flow for the servicing of loans was important. Profits were not too important. The Koreans were in the game of catching up. They had to grow. All earnings must go into expansion. In no time at all the Koreans emerged as an economic powerhouse.
8. The foundation may seem weak but as long as they can grow and generate cash-flow they were safe. As the chaebols grew and expanded Korea prospered. The per capita income qualified Korea for membership of the OECD.
9. There was no doubt that Korea was a success story. Its way of doing business is obviously not the same as the mature economies of the West or even of Japan but it was an economic success. The people as a whole prospered, were well educated and quickly became highly skilled. There was no reason to think that if they continued to employ their strategy they would become a developed country fairly soon.
10. The Koreans may be said to be practising crony- capitalism par excellence. Apparently only a selected few benefited and emerged as great tycoons owning chaebols. But if others are given the same kind of selective support by the Government would they not be regarded as the Government cronies also? If a great many were to get the same support indiscriminately would the strategy work? The capacity of the Government would be much stretched and it is likely that none would really succeed. They would all be small or midsize companies which would not contribute towards Korean nationalistic developmental targets. Korea would be just like any other developing country, struggling for years to feed its people. The most talented or adventurous would migrate. The less enterprising would stay home in a perpetually developing country. But Korea created the tycoons and the chaebols and achieved tremendous growth to become a Newly Industrialising Country. It must be remembered that Japan did the same even more thoroughly during the Meiji Restoration.
11. In Southeast Asia the ASEAN countries decided to depend on foreign investments for their development and industrialisation. Unless the domestic markets are involved, the foreigners were free to do anything, including owning 100 percent of the industries. Their gains were less and slower in coming than in the Korean case. It took them a long time to acquire the technologies and the skills of industrial management and investments. It took them a long time to build up the capital they needed to grow big.
12. But eventually they did produce their smaller versions of the chaebols. Certain industries mainly those serving the local markets, were kept out of the hands of foreigners. When privatisation became acceptable the state enterprises and the big utilities were handed over to those local businesses which had grown big enough to handle these state-owned entities.

13. It must be remembered that most of the state-run businesses were moribund. They were regarded as the services to be provided by the state due to the taxes paid by the people. Thus the roads were built and maintained by the state for the use free of charge mainly, by the tax payers. No return was expected by the state. Since the state had inadequate funds the roads were badly constructed and even more badly maintained.

14. Privatisation removed most of the responsibility of the state to build and maintain roads. But since the state continues to collect taxes, the state must return the taxes to the people in some way. And so the state subsidises the construction and maintenance of the public utilities by selling off at a much discounted price. That way the charges, road tolls in the case of some of the highways, would remain low.

15. Again some people have to be selected for whatever enterprise or industry that the Government wished to promote. It does not matter who was selected, whether they are friends of the Government leaders or not; whoever gets selected for anything at all, will be labelled cronies of the Government. Even when public companies are selected the charges of cronyism would still be made. Just about any businessman who benefits in anyway from Government decision would be labelled a Government crony. That the selections were made through open tenders made no difference. They would still be considered as cronies.

16. Only if foreigners get the project unconditionally, without regard for national benefits would the accusation of cronyism not be made. The foreigners must be allowed to take everything for themselves without any restriction. Their claim is that they, because of their absolute superiority, were doing a favour to the countries concerned because they would provide the best services and goods at the best cost, not necessarily the lowest cost of course. That they make huge profits for themselves is totally acceptable even though they provide unfair competition for the locals.

17. In both Korea and Southeast Asian countries there is probably some degree of true cronyism and nepotism. There must be some who have been given opportunities and help because they were cronies or members of the families or connected. But it is not correct or fair to assume that everyone who had been 'favoured' were cronies. Even members of the families may have legitimacy in their dealings involving the Government.

18. Whether the practices and the strategies of these countries were good or bad, no one can say that they had failed to develop their countries well and fast, have given their people ever higher standards of living, increased their technological, educational and other skills and generally put them and their countries strongly on the path of progress way ahead of other developing countries. In fact left to themselves these countries would catch up with the developed countries in a relatively short-space of time.

19. Would these countries practising what they have been practising collapse

economically? They may not be able to keep up the pace, they will have hiccups. Some of their businesses and their banks would fail. But it is doubtful that they will suffer total collapse. Certainly not suddenly and simultaneously -- one moment hale and hearty and the next moment tottering aimlessly about in a state of total collapse.

20. Should anything happen to their bank or institution or business, no matter how big, efforts could be made to turn them around. Rescuing companies is something that everyone does. The idea that companies which fail must not be rescued is not a matter of religious injunction. Too many innocent people would be punished if businesses are allowed to fail. Punish the wrong doers by all means but killing the company serves no good purpose. The innocents would be the one to suffer most. And so if there are failures, the companies could be resuscitated and the country go on prospering. The countries of East Asia would not collapse suddenly and simultaneously. There would be no massive contagion, only some temporary flu.

21. But we know that the countries of East Asia suddenly collapsed together. If it is not because of their bad Governments, their corruption, their crony- capitalism and nepotism, then what?

22. They collapsed because their wealth was taken away from them, through their money being devalued. They collapsed because they were suddenly made extremely poor. They were not able to pay their debts, not able to borrow, not able to finance their business activities, not able to do anything. They were financially paralysed.

23. When their currency is devalued the cost of buying foreign currency to pay debts or to buy raw materials, components or services became unaffordable. Interest rates and credit squeezes do not help either. Simultaneous attacks on the share markets render the companies insolvent as banks call for margins. Non Performing Loans (NPL) increased.

24. The collapse is caused by currency being devalued. There may be other excuses but it is devaluation which precipitated the collapse. How does the currency get devalued? Did the currency sense that the Government was corrupt etc and decide to devalue itself? Obviously not. Did the Government devalue the currency? The Government obviously did not. Then who did? The currency traders did.

25. Why did they do it? Is it because they feared they would lose money? No. There is no evidence that they were holding large quantities of the currencies concerned. So a fall in the value of the currency was not going to cost them anything, neither would a revaluation give them any profit. But by borrowing the currency and then selling it they could cause the currency to depreciate. And when it had depreciated sufficiently they could buy the currency and deliver to those who had bought at the higher prices and so make handsome profits. No lack of confidence or fear of losing money on their investments are involved. It was the possibility of making huge profits through short selling that motivated the

currency traders. It was greed; a kind of greed that cares nothing for the destruction caused, for the collapse of perfectly healthy and prosperous economies, greed that thrives on the misery of others.

26. These currency traders control and manage huge funds invested in by the very rich in the very rich countries. On top of that they could leverage by, in the case of the Long-Term Capital Management Fund, up to 200 times. They are well connected. They are the cronies of the bankers who manage huge funds belonging to the public. They believe that if they are big no one can stop them from manipulating the market any way they wish. The Central Banks of developing countries with their puny reserves would be bankrupt long before they, the funds, have risked even a fraction of the huge sums at their disposal.

27. The fact that by devaluing the currencies they create financial turmoil, impoverish the countries and their people, throw millions out of jobs and deprived them of food, medicine etc, cause them to riot and destabilise previously stable Governments and even cause these Governments to be overthrown -- all these bothered them not a bit. They merely claim that these Governments were bad and they had lost confidence in them and so pulled out their money. That they had not invested at all in these countries and really did not have anything to pull out, did not bother them. That their loss of confidence would not cause them to lose anything also did not bother them. If the act of pulling out their money would earn them handsome profits, then they would borrow the money in order to pull it out. The important thing is to make money from the opportunity which they could create based on their alleged lack of confidence. If the fundamentals are good and there is no reason for losing confidence, then contagion can be a good reason for loss of confidence. Any reason is good enough for borrowing the currencies in order to pull out, to short-sell and to reap huge profits.

28. And so one after another the tiger economies of Asia had their currencies devalued by the currency traders and all their Governments were accused of corruption, nepotism, crony capitalism and mismanagement. Everything they had done before which enriched and developed their countries were now blamed for creating the loss of confidence, and the devaluation of their currencies. The whole world joined in the chorus, accusing the Governments of East Asian countries of causing their countries to descend into financial and economic turmoil.

29. No mention was made of the role of the currency traders except that they had lost confidence and like herds of cattle they rushed off with their money. This is their right. Why should they put their money at risk? They invested in order to make money, not to prop up corrupt Government. But one might point out that they never really invested in these currencies. That is irrelevant. Since they saw an opportunity to make money by borrowing the currency, selling it down and profiting by it, why not?

30. They also attack the stock market, selling off the shares they hold or the share they borrowed. The share indices plummeted. The companies lost their capital and became unable to meet margin calls or pay debts. The share value

went below the asset value. These companies can be bought for a song. They no longer pay the Government any tax on their profits. They were not making any profits. They were losing. The Government cannot make ends meet now.

31. Here is where the IMF comes in. Loans are offered on condition the countries allow foreign companies to acquire businesses or start businesses without any condition. Other conditions imposed such as higher interest rates and credit squeezes ensured that more banks and companies go into failure. The turmoil worsened. But not to worry. The companies and banks failed because they were bad and should be got rid off. Only good companies would remain and when the economy recovers it would be healthier. But the currency refused to recover. It became worse instead.

32. Eventually the IMF is blamed. Still the currency traders are not blamed. They were left free to rape other countries. So long as they do not disturb the economies of the rich countries no blame was attached to them.

33. Feeling safe and not being conscience-stricken by the tragedies they have wrought all over the world, the fund managers grew bolder. They borrowed more and they directed their attacks against every country that they could make profits from. Only the countries where their main investors like were left free.

34. But then Russia collapsed totally under their attacks and the Russian Rouble became totally useless. The Long-Term Capital Management Fund lost a huge sum of money. Nobody really knows how much they lost as transparency is demanded by them only of others but not of themselves.

35. But transparent or not the lenders to the fund cannot hide the huge losses they had sustained. We know some of these individual losses by banks and various funds exceed billions. We know that the Fed had to force banks to bail out the LTCM with some 3.5 billion dollars. But we will never learn the full story because surreptitious rescues are being mounted to bail out the others. The investors in the LTCM are VIPs and unlike the millions who are starving in the poor countries raped by the funds, they must be saved.

36. Cronyism is extensive in the operations of the banks and the funds. They all know each other and they talk all the time to each other. In many instances they had previously worked together in the same institutions or companies. Subscription to the funds are by invitation only and obviously those invited are known to the managers of the funds. Although the funds may compete with each other, there are enough indication that they also collude.

37. Whenever any currency is sold, there must be someone who bought. If buying a currency would revalue it, then it should be revalued as often as it is devalued. There cannot be any sale without any purchase. There must always be a willing buyer and a willing seller. They would neutralize each other. But it would seem that sometimes there were only sellers who devalue the currency without there being any buyers to revalue the currency.

38. Sometimes the market is thin i.e only very small amounts were being bought

or sold. Yet on the basis of these small deals the whole currency gets devalued or revalued. How can such small transaction result in billions being lost or gained by whole nations.? People, millions of them get impoverished, starved, lost access to medical treatment because a few people sold a small amount of currency in some faraway place.

39. The Governments of many East Asian countries may be bad, may practise cronyism, nepotism etc. They may provide an excuse for loss of confidence by the so- called market force. But these Governments did not devalue their currencies nor did the currencies sense the wickedness of the Governments and devalue themselves. The currency traders devalued the currencies by their speculation and manipulation. The IMF did not devalue but they helped the process and they provide additional excuses for the currency traders to devalue the currencies further. If the countries failed to implement the strictures of the IMF, then the currency traders would cause the currencies to devalue further. The IMF is not quite culpable but it used the threats of the currency traders to extract the maximum compliance from the subject Governments.

40. The currency traders are no doubt the people responsible for devaluing the currencies. They are the cause of the currency turmoil. They spread it worldwide. They precipitated the current recession in every country. They are well on the way to bringing about a worldwide recession.

41. If we are going to manage the Asian Financial crisis with any possibility of success we have to deal with currency speculation and manipulations.

42. It is said that the volume of currency trading is 20 times that of world trade. It is perhaps even bigger now. But what is there to show for the amount of money involved? World trade creates wealth and jobs and industries and all and every kind of economic activities. Without world trade good growth for any country would not be possible. The transportation industry, the shipping, air freighting, land transport of every kind, insurance, stevedoring and a host of other commercial activities would not be there without world trade. The world is as developed as it is today because of world trade in goods and services of every conceivable kind.

43. If world trade is 20 times its present value, then the wealth and the well-being it creates would be unimaginable. Every country, rich or poor, backward or advanced would be considerably enriched. But we know that the wealth of the world is due largely to the trade in goods and services, while currency trading despite being 20 times bigger has not contributed anything to the well-being of the world, to economic development. Indeed we know for a fact that currency trading has destroyed the economies that world trade had built, has impoverished millions and now threatens to cause a world depression. A few very rich investors may have made huge profits for themselves from the trading in currencies by the so-called hedge funds but their combined profits could add up to only a fraction of the amount of wealth they have destroyed. And now we see that they can fail too and drag down with them the rich investors, the banks and other hedge funds. Despite bailouts the collapse of just one hedge fund

involved in currency trading is likely to cause worldwide recession.

44. It is clear that currency trading has not done any good for the world, in fact has been the cause of the present financial and economic turmoil, has impoverished the world. Unless currency trading is recognised as the root cause of the present problem, corrective actions cannot be made. Cosmetic adjustments, correcting peripheral causes etc will not do any good at all. Nor would an admission that currency trading is too big and too powerful to be regulated help overcome the problem.

45. Exchanging one currency for another is necessary for world trade. But currency trading in the present form is not essential. If currency trading cannot be done away with, then it should be properly supervised and regulated. This is possible if the big rich economic powers are willing to cooperate, to enact laws and rules and to enforce them.

46. Currency trading must be forced into the open. The world acted in concert to prevent money laundering. There is no reason why the world cannot act in concert to regulate currency trading.

47. Such trading must be registered and licensed in the countries where they operate. Banks must be made to reduce the money they lend to these funds to reasonable multiples. The basis for changing the exchange rate must be regularised. So long as there are buyers, there should be no change in the rates. Only a certain percentage in the change of exchange rates should be allowed for a given time. Any rate exceeding the percentage allowed should result in stoppage of trading. The sellers must deliver within a specified period the money sold. An amount not exceeding a certain percentage of the trade of the country concerned must be fixed as the maximum limit for any deal on any day.

48. Obviously the rules and regulations and laws will prevent the traders from making the kind of profit they are used to making. But if trade in goods and services are limited by what the market can bear, why should it not limit trade in currencies? Must we protect the excessive profitability of currency trading to the extent of plunging countries, regions and the world into economic turmoil and recession?

49. Free trade is good only if it brings about wealth and benefits to the peoples and the countries involved. Free trade is not meant to profit one at the cost of the destruction of the other partner. If free trade means that the rich can rape the poor, then we might as well resort to conquest and colonisation of the poor by the rich and the powerful. If this is what the world economic order is going to be like, then we might as well not talk about the independence of nations and human rights. It would be the height of hypocrisy if we accept the exploitation of the poor by the rich as the norm, when we all talk about a brave, humane new global society. We are actually backsliding and returning to the Dark Ages, the age of superstition in which economic and political exploitation must be subscribed to by everyone on pain of being declared a non-believer and being burnt at the stake.

50. You are going to discuss the management of the Financial Crisis. You are going to identify the lessons and the challenges. I am sure you are not indulging in an academic exercise. Pussy footing around will get us nowhere. You will have to face the problems squarely and be willing to accept the condemnation of the rich and the powerful if your conference is to contribute anything at all to the solution of the financial crisis faced by the world. I hope you are willing to face up to the challenge.