Asian Crisis Essay, Research Paper

Asian Crisis

The financial crisis that erupted in Asia in mid-1997 has led to sharp declines in the currencies, stock markets, and other asset prices of a number of Asian countries. It is hard to understand what these declines will actually do to the world market. This decline is expected to halve the rate of world growth in 1998 from the four percent that was projected pre-crisis to an estimated outcome of about 2 percent. The countries that are included in the East Asian crisis, known as “Tiger” economies, are Hong Kong, Indonesia, South Korea, Malaysia, the Philippines, Singapore, Taiwan and Thailand. For these countries to participate effectively in the exchange of goods, services, and assets, an international monetary system is needed to facilitate economic transactions. To be effective in facilitating movement in goods, services, and assets, a monetary system most importantly requires an efficient balance of payments adjustment mechanism so that deficits and surpluses are not prolonged but are eliminated with relative ease in a reasonably short time period. The Asian crisis of recent falls into this category of inefficient balance of payments facilitated by depreciation of its currency. By competitively depreciating its currencies, Asia is exporting its deflation, its overcapacity and its lack of growth to the West, particularly to the US. History The past ten or fifteen years have seen an unprecedented expansion in the extent to which the countries of the world are tied together, both by instant communication and by international trade, institutions, and markets, including financial markets. On the whole, this process of globalization has been an enormously positive development. It has opened new markets, enhanced competition, spurred innovation, and provided new opportunities for workers, farmers, and businesses around the world. For example more than 40 percent of US exports today are absorbed by developing countries, an extraordinary increase over past export patterns, and the jobs associated with these exports are high-paying, good jobs. The increasing productivity of our trading partners has helped keep inflation down and improve standards of living in the United States. And outside the US, probably hundreds of millions of people have been lifted out of poverty around the world by the economic growth and trade over the past twenty or thirty years. Effects of the Global Economy In this new global economy, countries are more tightly linked than ever before to each other’s fates. A decade ago, a collapse in the currency of a small, distant country like Thailand would barely have rated a mention in the typical American newspaper. Last year, however, that currency crash triggered a crisis in other East Asian countries that has dominated news coverage in a way that no other foreign financial crisis has ever done before in this country. The reason for the change is that we now have more at stake than ever before in the economic performance of these countries. Not only are they major customers for our products; the rich countries and developing countries are also increasingly linked by financial ties. In 1996, the developed countries including the US invested more than 250 billion in emerging markets, and this is compared to roughly 20 billion ten years earlier. Much of this money was from banks (especially in Japan and Europe), although US mutual funds, pension funds, and individual investors also participated. But whatever its source, the extent of this investment means that economic turmoil in East Asia has a direct financial impact on the developed world’s capital markets, including our own. Indeed, a brief plunge in US stocks last October was widely attributed to turmoil in the Hong Kong stock market that was, in turn, linked to the crisis set off by Thailand’s currency crash. What were the causes? Throughout the East Asian crisis many different ideas have been proposed to what the cause or causes were. Attempts to identify the fundamental causes of a financial crisis always suffer from the problem of distinguishing insight from hindsight. Many financial journalists today have said the the crisis was the inevitable counsquence of: “overvalued exchange rates, large current account deficits, short-term capital inflows, opaque financial systems, or one of several other supposedly fatal flaws in East Asian capitalism.” It seems fair to say that a year ago nobody suspected that a calamity like what we have seen was possible, although all of the characteristics that are now described as the fatal flaws of the East Asian economies were reasonably widely understood even then, at least by experts.

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