

# The Global Economic Crisis

## What It Means To Asia



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# Introduction

## Asia and the Crisis

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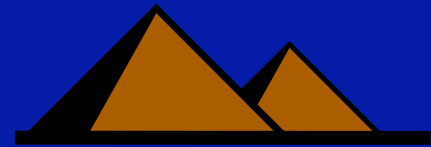
- The current financial crisis and global economic downturn did not originate in Asia.
- Structurally, Asian countries are generally in good shape.
- Asian economies and financial markets have nonetheless been impacted at varying degrees.
- Effects are likely to deepen substantially over the coming year.

# Origins of the Crisis

## The US Financial Meltdown

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- Subprime loans yet another one in a series of asset bubbles (S&L, dotcom)
- Liberal US housing policy
  - loans to NINJAs
- Housing pyramid: loans were lucrative on both sides, until...
- Spreading of risk mistaken for reduced risk
- Moral hazard: Uncle Sam to the rescue (same moral hazard led to Asian crisis)



# Origins of the Crisis

## Global Savings Imbalance

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- Americans consumed too much (fueled by lucrative mortgages)
- Asians saved too much? (Bernanke's lament)
  - Bought complex financial assets built on subprime loans
  - Sold Americans their export products (incurring large trade surpluses)

→ **So whose fault was it?**

# Effects of the Crisis

## A Threefold External Shock

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- Financial turmoil
- Recession/slowdown in major Western Economies (US, Europe)
- Adverse relative price movements

# Effects of the Crisis

## A Threefold External Shock

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- **Financial turmoil**
  - \_ Tight credit access for governments, businesses
  - \_ Falling stock markets: diminished business confidence
  - \_ Adverse exchange rate movements: more volatility; unwanted strengthening

# Effects of the Crisis

## A Threefold External Shock

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- **Recession/slowdown in major Western Economies**
  - \_ Reduced exports & tourism
  - \_ Lower FDI
  - \_ Slower/lower remittance flows
    - Loss of jobs, rise in poverty
  - \_ Pressures on government finances  
(\_T, \_G)

# Effects of the Crisis

## A Threefold External Shock

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- **Adverse relative price movements**
  - \_ Higher oil prices
  - \_ Higher food prices
    - (have since moderated)
  - \_ Weaker export commodity prices



# Hardest hit Asian economies:

	%Exp/GDP	GDP g.r.
• Singapore	231	-16.4
• Japan	18	-12.7
• Thailand	73	-4.3
• China	41	6.1
• India	21	5.3

→ *Most of Asia still expected to grow*

# Most of Asia still not as hard hit because:

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- We've had "practice" in 1997-98
  - Financial sector better regulated
  - Less exposure to complex financial assets from US
- Asian economies have been fundamentally sound
  - High forex reserves, saving rates
  - Healthy government finances
  - Trade (current account) surpluses

# Still, crisis is still deepening in the West, and effects on Asia could intensify

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## L, U or V-shaped recovery?

- V can be safely ruled out
- Bernanke's "green shoots" and Obama's "glimmers of hope" dispelled by latest developments
  - "Good news" merely means rate of decline slowed, but still falling
  - Announced bank profits more the result of accounting technicalities
  - Numbers have turned bad anew

# The Challenge:

- Measures for **short-run stabilization** may take a toll on **human welfare** and **long-run sustainability** (financial stability vs. sustainable human development?)
- Financial markets: “Heads you win, tails I lose” situation for vulnerable sectors

# Human Costs

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## Increased poverty

- Higher unemployment
- Increased school drop-outs
- Increased hunger, malnutrition and sickness

# Human Costs

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## Reduced social investment

- Budget cuts on social services
- Public investments in human development
- Higher cost of/reduced private provision of social services

# Human Costs

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## Damage to social capital

- Rise in
  - Crime incidence
  - Domestic violence
  - Child abuse
  - Street children
- Breakdown in community cohesion

# Environmental Costs

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## Reduced environmental investment

- Low priority for environmental investments
- Shelve planned investments in environmentally sound technologies
- Non-operation of existing environmental equipment



# Environmental Costs

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## Easing of environmental standards

- Relaxed policies and standards
- Non-enforcement of existing ones
- Pressure on environmentally-sensitive exports

# Environmental Costs

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## Adverse migration impacts

- Increased pressure on uplands & coastal areas (“Environment is the SSS of the poor”)

# Asian Responses to Past Crises

## Households

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- Increased labor force participation
- School drop-outs
- Changes in consumption patterns
- Migration
- Donation of personal gold/jewelry to government reserves

# Asian Responses to Past Crises

## Firms

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- Moratorium on strikes/layoffs
- Wage hike postponement
- Salary/allowance cuts
- Voluntary unpaid leaves  
("Spreading out the work")
- Liquidation of non-essential assets

# Asian Responses to Past Crises

## Governments

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- Increased taxes, borrowing
- Budget cuts, reprioritization
- Capital controls (Malaysia)
- Leverage private/community initiatives

### Longer-term:

- Financial sector reform
- Social safety net systems

# Asian Responses to Past Crises

## Governments

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- Impact monitoring system
- Unemployment safety nets
- Skills training, emergency employment, job matching
- Focused social services
- Income maintenance programs (e.g. targeted food/fuel subsidies)

# Response to Crisis (Then & Now)

## International Institutions

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- Liquidity & budget support
- Social safety net support
- Support/advice on:
  - impact monitoring systems
  - effective & efficient targeting mechanisms
  - public-private partnerships in public investments

# Current Imperatives for Asia

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- Fiscal stimulus, subject to fiscal sustainability), with emphasis on social & environmental expenditures
- Rethink past export-driven growth strategy: “Rebalancing growth”
  - Boost investment spending
  - Greater intra-regional trade
- Stronger regional cooperation
  - Widen financial cooperation
  - Closer regional economic integration



# Asia and the West

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- Asia has much to learn from the West
  - Avoid pitfalls of excessive financial deregulation
- Asia has much to give to the West
  - Large reserves; continued growth (and market expansion)
- Asia has much to teach the West
  - Inherent sustainability in Asian cultures & indigenous knowledge

# Can Asian economies save the global economy?

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- High rate of savings
- Huge foreign exchange reserves
- Fiscal space to undertake stimulus
- Large and expanding market for products of the West

# Can Asia bail out the world?

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Reality Check:

Countries	GDP Trillion \$
USA	13
Europe	12
Japan	4.2
China	3.2
ASEAN	1.4
India	1.2
Asia	10

**→ US & Europe must fix themselves!**



Thank You!