

**Asia and the Global Economic Crisis: Challenges in a Financially Integrated World by John Malcolm Dowling and Pradumna Bickram Rana, Palgrave-Macmillan, 2010. £ 65, pp 271**

*“...An important lesson from the Asian Financial Crisis was that in order to manage financial globalization, policy actions was required at the national, regional, and global levels. But V-shaped recovery resulted in complacency and reform measures were quickly forgotten. This partially set the backdrop for the present global economic crisis.....”*

Berry Deskar

This book authored by two experts on Asian affairs, takes the policy actions implemented by countries to manage financial globalization and identifies the remaining agenda to be finishing in order to avoid reoccurrence of such crisis. Drawing upon the rich set of data and references, this book provides a timely account of the impact of the global recession on Asian economies, the way by which policy makers were facing. It describes origin of Global Economic Crisis (GEC) in the US and deals with the responses of the US and Europe and moves on quickly to focus on its spread to Asia and especially on Asia's reaction/policy responses to it. The authors have examined the current GEC in the perspective of the Asian region, reviewing how different regions of Asia were affected, and identifies the challenges that Asia faces in a financially integrated world. Further, it analyses the impacts of the policy responses adopted and the persisting challenges in rebalancing the global economy, the next steps in regional economic integration in Asia, and issues related to reform of the international financial architecture. It discusses Asian and global initiatives for rebounding growth, highlights the impact of the crisis on poverty and the millennium development goals, and provides a detailed analysis of individual country responses and prospects. As the world emerges from the crisis, the authors assess what has been achieved so far, where Asia stands at the beginning of the new decade and what more needs to be done to successfully manage financial globalization in the future.

The book covers the topic in twelve chapters starting with chapter 1. Introduction, 2. The Crisis and How it Unfolded in Industrial Countries, 3. Transmission to Developing Countries in Asia, 4. Policy Responses – Asia, 5. Impacts of the Global Crisis on Asia and Outlook, 6. Policy Responses – Asia, 7. Where we Stand at the Beginning of 2010, 8. Asian and Global Initiatives for Rebalancing the Global Economy, 9. Impact of Crisis on Poverty and MDGs, 10. Individual Country Analysis and Prospects, 11. Economic Integration in Asia: Trends and Policies and 12. Reform on International Financial Architecture: Progress and Remaining Agenda.

With the financial globalization, large inflow and sudden reversal of private capital flow has increased. In such a crisis domestic investors also liquidate their assets. Since 1990s, there have been 10 episode of capital account crisis across the world. The lesson learned from the capital account crises that have occurred around the world so far in terms of managing the resolving and in trying to prevent a similar crisis from occurring in future in Asia. Cross border operation of many financial institutions had been contagion effect for GEC and requires coordination at global level as well as multilateral actions. The present crisis has triggered the debate over tighten policy regulations and G20 leaders are getting consensus to develop globally accepted set of policy regulations to improve the quality and quantity of bank capital to implemented by 2012. As the idea of World Finance Organization (WFO) is emerging to meet international standards for supervision and regulation for financial market of member countries mandatorily at global level, the idea of establishment of Asian Financial Stability Board (AFSB) at regional level is also getting leveraged to be responsible for both micro-prudential as well as macro-prudential supervision apart from promoting financial stability in the region by developing and implementing early warning system (EWS) of banking crises and focusing on long-term financial market development and integration issues in the region.

The book is well thought-out in 12 chapters and focuses on anatomy of the crisis in the US and subsequently spread to the other

industrial countries and Asia. Analysis of the genesis of the crisis from several different perspectives is duly narrated in chapter 2 and finds that accommodative monetary policy of the Federal Reserve caused fall in prime lending rate from around 9 per cent in 2001 to 6 per cent by 2004 as the federal funds rate came down from 6 per cent in early 2001 to an all time low of 1 per cent by mid-2003. Lower interest rates and aggressive lending caused bubble in the housing market and development of the subprime mortgage market which resulted in a tripling of average home valued in less than a decade and an enormous windfall in wealth for home owners. The role of leverage, the lack of appropriate supervision of mortgage lenders and the role of derivatives, particularly mortgage securities are identified. Book has tried to dig out what went wrong and finds that animal spirit to create more assets with more opaque risk profiles and increasing their financial leverage, changes in policy regulations or no regulations such as repeal of the Glass-Steagall Act which allowed commercial banks to enter the investment banking business and take more risks, changes in structure of housing market causing to boom in housing sector and variable rate mortgage became more common and qualifying income requirement were ignored or fudged and misplaced belief in the riskiness of assets and the skill of rating agencies. The chapter, further, analyses the spread of the crisis to the industrial countries. Particular reference is made to the inter-linkages between banks and other financial institutions in the US and Europe that contributed to the contagion of the crisis.

Chapter 3 gives an account of the spread of the crisis to Asia through various channels. There were four major ways in which financial stress was transmitted. The first was investment by investor banks and mortgage companies in what would come to be known as 'toxic' assets that emanated from the subprime mortgage crisis in the US and UK. The riskiness of these assets increased and their prices fell when the mortgage bubble burst in the US and Asian holding these assets were adversely affected. Second, foreign direct investment and portfolio investment flows into developing

countries are also adversely affected. Third, as the global crisis deepened the demand for Asian Exports also began to fall and there were impacts on foreign exchange markets. The fourth channel was through remittances flows from Asian working in industrial countries to their families back home. The developing economies of Asia were most affected by a decline in demand for its exports as well as withdrawal of funds from equity market, creating stress throughout the region. In order to come out of the recession much will depend upon the shape and duration of the recession and recovery in the US.

The chapter 4 discusses the stimulus measures that were undertaken by the US to deal with financial crisis and economic recession, which includes tax incentives for businesses, income tax rebates for lower and middle-income group. As the crisis deepened, in September 2008, the US Treasury put Freddie Mac and Fannie Mae in conservatorship. It was assumed initially that monetary policy would not play much of a role in mitigating the crisis as interest rates were already low and monetary policy was relaxed. But Federal Reserve started buying assets and thereby injecting money into the system. Further, the chapter duly discusses the size and timing of fiscal monetary stimulus measures. Conventional monetary easing including interest rates and reserve requirements as well as other quantitative easing measures are discussed. Fiscal stimulus including tax and spending measures are delineated including the size, time and scope of these measures in industrial countries is discussed.

The thorough impact on Asia and its responses to the crises are discussed in chapter 5 and chapter 6. The former chapter develops taxonomy for analyzing economic developments in the Asian region. Several country groups are developed based on country size, level of development and degree of globalization. The three large economies of China, India and Indonesia are one group. Another group comprises richer countries of Southeast Asia and East Asia. The poorer countries that are less integrated in the global economy are grouped together and a final group comprises three countries in southeast Asia that are sandwiched between the other richer

countries in East Asia and poor countries in south Asia. In Chapter 6, differences in responses for different countries are reviewed and size of fiscal stimulus as a percentage of GDP is compared. Monetary stimulus measures were designed to provide liquidity to the economy and also to stimulate investment. Accordingly, most Asian countries have implemented measures to relax monetary policy and encourage bank lending. Monetary policy stance of various Asian countries are also reviewed as well as additional details of forecast for domestic demand, government budgets, current account, capital flows, unemployment and remittance flows.

A snapshot of the region as of early 2010 is provided in Chapter 7 including perspectives on the length of the recession, comparison with other recessions in Asia and the outlook for 2010. The recovery path of Asian countries through 2009 and early 2010 has been consistent with projections made by various international agencies. Loss of income resulting from the recession is estimated and these losses are compared with losses sustained during Asian Financial Crisis. Further analysis of poverty and unemployment are discussed in detail.

Suggestions for Asian and global initiatives to rebalance the global economy are discussed in Chapter 8. A return to the status quo of high saving and export-led growth by Asian economies combined with large US current account deficit and low saving rates is not plausible. Focus is given on two aspects of rebalancing the global economy. First, it explores the possibilities of coordinating fiscal stimulus measures in order to facilitate the unwinding of asset positions and the adjustment of international borrowing and lending and second, it explores how developing countries with large surpluses reduce their saving rates while increasing domestic consumptions, which is an important step to follow the policy coordination measures to develop a coordinated stimulus.

Chapter 9 examines the expected impact of the crisis on poverty in Asian economies. Reference is made to the Asian financial crisis and estimates of the impact on the Millennium Development Goals.

The analysis of poverty and growth in 2009 and 2010 is discussed in chapter 10 where individual country experiences and measures are discussed in more depth. Poverty and unemployment are discussed within a framework of expected macroeconomic and international trade developments. Only the countries of the region which are expected to have significant poverty impacts are discussed. This leaves out the richer countries in East Asia.

The Asian Financial Crisis had ignited Asia's interest in promoting regional economic integration. Chapter 11 argues in the context of economic integration in Asia and says that the global economic crisis has further strengthened the case for Asian regionalism. It prescribes list of suggestions for trade integration, financial integration, macroeconomic policy coordination, economic review and policy dialogue and regional financing arrangement. It also discusses the various efforts that have been made and indentifies the next steps in the region's economic integration.

Chapter 12 discusses rehabilitation efforts that are being made for crisis prevention, resolution and management. As Asian Financial crisis was triggered by capital account factors associated with financial globalization. The policy measures suggested by IMF in managing Asian Financial Crisis were not appropriate. With the V-shaped recovery, complacency had set in and the reform measures were quickly forgotten and progress was, however, limited because of the region's V-shaped recovery. It cautions that failure to reform the international architecture could sow the seeds of the next crisis in the future. It sets a list of prescription for crisis prevention such as standards and codes, data transparency, financial system soundness and surveillance and capital account deregulation. However, in order to manage crisis, it suggests new financing instruments and credit lines, IMF conditionality, private sector involvement and reforms of IMF governance. The book finds it too early to fully assess the impact of the post-GEC efforts under the auspices of G-20 but says there is once again the possibility that the faster than expected

recovery from GEC could lead to compliancy. If so, vulnerability to future crises would remain. But authors are optimistic that it will not happen this time around as the process is now being led by the G20 and developing countries are important stakeholders in this process.

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