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SEPTEMBER 11, 2001

WORLD BANK, HONG KONG MONETARY AUTHORITY, PACIFIC ECONOMIC COOPERATION
COUNCIL (PECC) CONFERENCE ON EAST ASIAN FINANCIAL COOPERATION

ON BEHALF OF THE CO SPONSORS - A WARM WELCOME TO YOU ALL AND A SPECIAL
WORD OF THANKS TO FINANCIAL SECRETARY IP FOR THE AUSPICIOUS START OF THIS
MEETING.

30 YEARS AGO PRESIDENT NIXON SUSPENDED CONVERTIBILITY OF THE DOLLAR INTO
GOLD, EFFECTIVELY ENDING THE POST WORLD WAR BRETTON WOODS CURRENCY
ARRANGEMENTS. I CHAIRED THE US SENATE HEARINGS ON THAT DECISION.

THE TESTIMONY PAID LITTLE HEED TO THE CONSEQUENCES FOR CENTRAL BANK
RESERVES OR THE CURRENT AND CAPITAL ACCOUNTS OF OTHER NATIONS.

THE US TREASURY SECRETARY, ANOTHER FORMER TEXAS GOVERNOR, REMARKED:
"IT'S OUR CURRENCY. THEIR PROBLEM."

WITNESSES ASSUMED MOST COUNTRIES WOULD ADOPT FLOATING EXCHANGE RATE
REGIMES AND, BY AND LARGE, FORESAW LITTLE INSTABILITY OR EFFECT ON REAL
ECONOMIES. LOOKING BACK, THEY DEMONSTRATED THE FALLIBILITY OF
CONVENTIONAL WISDOM AND THE DIFFICULTIES WE FACE TO DAY IN FORESEEING THE
FUTURE. IT IS MORE READILY INFLUENCED, FOR BETTER OR WORSE, THAN PREDICTED.

ALL BUT THREE ECONOMIES IN EAST ASIA LINKED THEIR CURRENCIES TO THE DOLLAR
WHICH, OF COURSE, WAS NO LONGER LINKED TO ANYTHING.

EXPERTS TESTIFIED, AS THEY STILL DO, THAT A WEAKENING DOLLAR WOULD
IMPROVE THE US TRADE BALANCE. BUT INSTEAD OF GOING DOWN, THE US TRADE
DEFICIT TOOK OFF.

IT WAS AMERICA'S CURRENCY, BUT IT WAS BECOMING AMERICA'S PROBLEM, TOO.

THE MOST PRESCIENT OBSERVERS 30 YEARS AGO MAY HAVE BEEN A HANDFUL OF
COMMODITIES TRADERS IN CHICAGO. THEY CREATED A THRIVING MARKET IN
FINANCIAL FUTURES TO HEDGE NEW RISKS. LATER HEDGE FUNDS WOULD CREATE
NEW RISKS, DESTABILIZING FINANCIAL MARKETS, EVEN HERE IN HONG KONG.

THE LATIN AMERICAN DEBT CRISIS FOLLOWED THE OIL CRISIS OF THE 70'S.

THE PLAZA ACCORD FOLLOWED IN 1985. THE DOLLAR WAS TALKED DOWN, THE YEN UP
- JAPAN USUALLY WENT ALONG. WITH MOST CURRENCIES PEGGED, EXPORTS FLOWED

OUT OF EAST ASIA; MONEY FLOWED IN.

BETWEEN 1992-3 THE COUNTRIES OF THE EUROPEAN MONETARY SYSTEM SPENT ALMOST \$200 BILLION TRYING TO SUPPORT TEN EUROPEAN CURRENCIES.

IN 1995, MEXICO WAS RESCUED FROM ITS CURRENCY CRISIS BY A US LED EFFORT. THE MEXICAN ECONOMY CONTRACTED BY 6 PERCENT.

BUT IT WAS NOT UNTIL 1997 THAT THE VOLATILITY OF THE POST BRETTON WOODS ORDER WAS APPARENT - AND THE VULNERABILITY OF EAST ASIA. UNTIL THEN COUNTRIES HAD BEEN RESCUED BY LENDERS OF LAST RESORT - OR HAD MANAGED THEIR WAY OUT, AS IN EUROPE IN 1992-3 AND THE US DURING ITS SAVINGS AND LOAN CRISIS OF THE LATE 80'S. MANAGED - BUT ALWAYS WITH DAMAGE TO REAL ECONOMIES AND HUMAN LIVES.

IN EAST ASIA CAPITAL ACCOUNTS HAD BEEN LIBERALIZED. CURRENT ACCOUNTS WERE OFTEN IN SURPLUS. FISCAL POLICIES WERE ON THE WHOLE PRUDENT. SAVINGS LEVELS WERE HIGH. THE INTERNATIONAL COMMUNITY HAD APPLAUDED, AND MONEY WHICH HAD POURED IN, POURED OUT.

IN 1993, PECC CREATED ITS FINANCIAL MARKETS DEVELOPMENT PROJECT (FMD). WE DID NOT FORESEE THE EVENTS OF 1997, BUT WE DID RECOGNIZE THE REGION'S EXCESSIVE DEPENDENCE ON COMMERCIAL BANKS. THEY WERE AN INEFFICIENT MEANS OF MOBILIZING AND ALLOCATING THE IMMENSE LIQUIDITY BUILDING THROUGHOUT THE REGION. MANY BECAME - AND REMAIN - INSOLVENT.

BY THEN EUROPE WAS WELL ON ITS WAY TO ACHIEVING A COMMON MARKET, MONETARY UNION AND A NEW RESERVE CURRENCY FOR THE WORLD.

BUT NOT EAST ASIA. THAT YEAR, AT THE FIRST MEETING OF APEC LEADERS PRESIDENT CLINTON INADVERTENTLY REFERRED TO A COMMON MARKET IN THE PACIFIC. EAST ASIANS, WITH AN UNCHARACTERISTIC LACK OF RESTRAINT, REACTED WITH HORROR. PRIME MINISTER MAHATHIR'S VAGUE TALK OF AN EAST ASIAN CAUCUS WAS GENERATING LITTLE ENTHUSIASM. ONLY AT THE SUBREGIONAL LEVEL WAS REGIONALISM EMBRACED. ASEAN AND AFTA SHOULDERED ON.

WHAT HAPPENED NEEDS NO RETELLING. BETWEEN 1990 AND 1998 JAPAN LOST ABOUT \$15 TRILLION IN STOCK AND PROPERTY MARKET VALUES. IT WAS LEADING THE FLOCK LIKE THE PROVERBIAL GOOSE. WHEN THE FLOCK'S TURN CAME IN 1997, THE WESTERN DOMINATED INTERNATIONAL COMMUNITY DID NOT RESPOND AS IT HAD IN MEXICO - AND IN RUSSIA - AND DOES TODAY IN TURKEY.

THE US HAD EMPLOYED ITS EXCHANGE STABILIZATION FUND TO RESCUE MEXICO, BUT NOT THAILAND. INSTEAD, IT JOINED WITH THE IMF TO PRESCRIBE TRADITIONAL CURES OF DEVALUATION, BUDGET CUTS, HIGH INTEREST RATES AND A VARIETY OF STRUCTURAL MEASURES ALL OF WHICH MIGHT HAVE BEEN APPROPRIATE FOR CURRENT ACCOUNT CRISES, BUT ASIANS WERE FACING CAPITAL ACCOUNT CRISES. IMF CONDITIONALITIES EXACERBATED CONDITIONS WHICH SPREAD LIKE A CONTAGION EVEN TO SOME OF THE WORLD'S BEST MANAGED ECONOMIES, LIKE HONG KONG AND SINGAPORE. THE NEW YORK FEDERAL RESERVE BANK ORCHESTRATED A BAILOUT OF LONG TERM CAPITAL MANAGEMENT TO PROTECT THE US BANKING SYSTEM. THE

DANGERS OF MORAL HAZARD AND CRONY CAPITALISM ARE NOT, IT SEEMS, CONFINED TO EAST ASIA.

AT THAT TIME JAPAN'S PROPOSALS FOR A MONETARY FUND TO UTILIZE THE REGION'S RESOURCES FOR ITS PROTECTION AND DEVELOPMENT WERE OPPOSED BY THE US AND CHINA. A NEW GLOBAL FINANCIAL ARCHITECTURE WAS PROMISED BY PRESIDENT CLINTON, BUT IT NEVER REALLY MATERIALIZED, EXCEPT FOR AN IMF FACILITY AND THE FAMILIAR EXHORTATIONS ABOUT TRANSPARENCY, IMPROVED REGULATION AND CORPORATE GOVERNANCE WHICH, HOWEVER OBVIOUS, PUT THE BURDEN ON THE DEBTORS WITHOUT ADDRESSING THE UNDERLYING VULNERABILITY OF SMALLER ECONOMIES, THEIR CURRENCIES AND MARKETS, TO EXTERNALITIES BEYOND THEIR CONTROL AND MAKING.

ECONOMIES WHICH RESISTED WESTERN ORTHODOXY AND CONTROLLED THEIR CAPITAL ACCOUNTS WERE RELATIVELY UNSCATHED BY THE CONTAGION.

WHAT HAVE WE LEARNED FROM THOSE 30 UNRULY YEARS? PECC FMD REACHED A CONSENSUS IN 1998. I DARE NOT SPEAK FOR SOOJIL YOUNG OF KOREA, YUICHIRO NAGITOMI OF JAPAN AND ALL MY ESTEEMED COLLEAGUES, LET ALONE OUR PARTNERS IN THE WORLD BANK AND HONG KONG MONETARY AUTHORITY. BUT I BELIEVE WE LEARNED THAT DEVELOPMENT OF FINANCIAL MARKETS REQUIRES REGIONAL INTEGRATION AND SOME KIND OF REGIONAL FINANCIAL OR REGULATORY ARCHITECTURE TO ENABLE REGIONAL LISTINGS, RATINGS, TRADING, SETTLEMENT AND CLEARING PROCEDURES - THE LIQUIDITY REQUIRED OF MODERN FINANCIAL MARKETS. THE STABILITY OF CURRENCIES, LIBERALIZATION OF CAPITAL ACCOUNTS AND TRADE FACILITATION REQUIRE CURRENCY REFORM, PERHAPS AN ASIAN CURRENCY UNIT (ACU) AND A REGIONAL MONETARY ARCHITECTURE FOR COORDINATION, SURVEILLANCE, LENDER OF LAST RESORT FINANCING - INSULATION FROM THE EXTERNALITIES THAT ARE POLITICAL, AS WELL AS FINANCIAL. FIXED, FLOATING, MANAGED, DOLLARIZED CURRENCIES - EVERYTHING HAS BEEN TRIED SOMEWHERE. AND NOTHING HAS REALLY WORKED, AT LEAST NOT IN THE SMALLER ECONOMIES.

CORPORATE REORGANIZATION AND BANK RECAPITALIZATION ARE PROCEEDING, ALBEIT UNEVENLY. EAST ASIA IS REFORMING. BUT, NOTWITHSTANDING MONETARY RESERVES EXCEEDING THOSE OF NORTH AMERICA AND EUROPE COMBINED, EAST ASIAN ECONOMIES WILL REMAIN VULNERABLE, INTRA REGIONAL TRADE AND INVESTMENT RETARDED, THE REGION FORCED TO RECYCLE ITS SAVINGS THROUGH FOREIGN INSTITUTIONS - UNLESS THERE IS SOME GREATER MEASURE OF REGIONAL FINANCIAL COOPERATION.

WITHIN ANOTHER 30 YEARS CHINA, GIVEN A CONSERVATIVE 6% ANNUAL RATE OF GROWTH, WILL PROBABLY ACQUIRE THE WORLD'S LARGEST ECONOMY, NO MATTER HOW IT IS MEASURED. WHERE WILL CHINA FIT? WILL CHINA SAP THE VITALITY OF ITS NEIGHBORS IN SOUTH EAST ASIA, SIPHONING OFF INVESTMENT, OR BE A LARGE SOURCE OF MARKETS AND CAPITAL FOR A DYNAMIC EAST ASIAN ECONOMY AND, INFERENTIALLY THE WORLD? CHINA, AND CHINESE TAIPEI, ARE EXPECTED TO ACCEDE TO THE WTO NEXT YEAR. A REGIONAL FINANCIAL ARCHITECTURE WITH JAPAN AND CHINA INTEGRATED, THE REMNIMBI FULLY CONVERTIBLE, COULD BECOME THE THIRD LEG OF THE WORLD'S MONETARY STOOL, AS WELL AS A SOURCE OF ECONOMIC VITALITY IN EAST ASIA. THEN THERE WOULD BE A NEW GLOBAL FINANCIAL

ARCHITECTURE.

WE DO NOT PRESUME CLAIRVOYANCE NOR TO KNOW THE ANSWERS TO THE MANY QUESTIONS RAISED BY THESE PROPOSITIONS. WE IN FMD CONCLUDED THAT THEY DESERVED A PROCESS FOR DISCUSSION, RECOGNIZING THAT BY 2005, AT THE LATEST, EUROPE WILL HAVE DEFIED ITS SKEPTICS TO CREATE A VAST CONTINENTAL FINANCIAL MARKET SPURRING ITS INTRA REGIONAL TRADE, INVESTMENT AND INTEGRATION OF BUSINESSES.

PECCFMD TEAMED UP WITH THE WORLD BANK TO FORM THE PROJECT OF WHICH THIS MEETING IS A PART, ITS PURPOSE TO BRING PRACTICAL EXPERIENCE AND PRIVATE SECTOR INTERESTS INTO THE BLOOD STREAM. WE HOPE TO DEVELOP INFORMATION, IDEAS, MOMENTUM. AND CONTRIBUTE TO AN EAST ASIA WHICH IS A PILLAR OF GLOBAL DYNAMISM AND FINANCIAL STABILITY AND NEVER AGAIN A SOURCE OF INSTABILITY.

IT IS NOT TOO SOON. LAST YEAR CHINA PROPOSED A FREE TRADE AREA FOR EAST ASIA. THE REACTION WAS SYMPATHETIC, IF SKEPTICAL AS TO FEASIBILITY IN THE FORESEEABLE FUTURE. MORE FEASIBLE MAY BE A REGIONAL FINANCIAL ARRANGEMENT. FREE TRADE AREAS ARE PREFERENTIAL AND DIVERSIONARY. THEY MAY UNDERMINE INTERNATIONAL INSTITUTIONS. THE DIVERGENCES IN EAST ASIA ARE EXTREME. BUT SINGAPORE AND BRUNEI HAVE A FUNCTIONING MONETARY UNION. MONEY IS DIFFERENT. IT PANICS, UNLIKE GOODS AND SERVICES. FINANCIAL REGIONALISM COULD FACILITATE TRADE AND EVENTUALLY A FREE TRADE AREA. CHINA'S PREMIER NOW SUPPORTS AN ASIAN MONETARY FUND.

THE MANILA FRAMEWORK, CHIANG MAI INITIATIVE AND BI LATERAL SWAP AGREEMENTS INDICATE MOVEMENT, AS WELL AS BROAD SUPPORT, FOR FINANCIAL REGIONALISM. ASEAN PLUS 3 HAS CREATED A VISION GROUP TO HELP SHAPE THE FUTURE. CENTRAL BANKS ARE MEETING REGULARLY. BILATERAL INITIATIVES ARE BEING CONSIDERED. AND ATTITUDES IN THE WEST ARE MORE REALISTIC. AMERICANS HAVE DIFFICULTY RECONCILING SUPPORT FOR REGIONALISM IN EUROPE AND THE WESTERN HEMISPHERE WITH OPPOSITION IN THE EAST. TO THE CONSTERNATION OF MANY AMERICANS, OUR COUNTRY'S FLAGGING SUPPORT UNDERMINES THE WTO AND THE INTERNATIONAL ORDER WE HELPED CREATE. A REGIONAL EAST ASIAN FINANCIAL ARCHITECTURE COULD SUSTAIN IT. THE BILATERAL SWAP AGREEMENTS ACTUALLY REINFORCE AN IMF WHICH UNDER ITS NEW LEADERSHIP APPEARS SYMPATHETIC TO EAST ASIAN REGIONALISM. THE ASIAN DEVELOPMENT BANK IS A PRECEDENT. IT HAS A LONG RECORD OF COOPERATION WITH THE WORLD BANK.

BUT HOW TO GET FROM HERE TO WHERE?

WE HAVE TRIED TO PROPOUND THE ISSUES IN A WIDE RANGING, PROVOCATIVE AGENDA WHICH SHOULD GIVE YOU AMPLE SCOPE FOR EXPRESSION OF YOUR VIEWS.

WE IN PECC FMD ARE HONORED TO BE ASSOCIATED WITH THE WORLD BANK IN THIS ENDEAVOR AND WITH THE HONG KONG MONETARY AUTHORITY IN THIS MEETING- AND GRATEFUL FOR THE RESOURCES AND PATIENCE THEY HAVE CONTRIBUTED. WE ARE ALSO GRATEFUL TO THE CHUBB INSURANCE COMPANY FOR ITS GENEROUS SUPPORT OF THIS MEETING AND TO CATALYST INSTITUTE FOR PROVIDING SEED FUNDING TO FMD.

WE AND OUR CO SPONSORS ARE GRATEFUL TO ALL OF YOU WHO ARE HERE, NOT AS LISTENERS, BUT AS PARTICIPANTS, SEASONED PRACTITIONERS WITH A VAST EXPERIENCE TO SHARE. WE URGE YOU TO SPEAK UP IN THE FREEWHEELING SESSIONS WHICH FOLLOW.

FOR THOSE OF YOU INTERESTED IN CONTINUING THE INVOLVEMENT, FMD WILL HOLD A MEETING TO REVIEW ITS AGENDA AND MANAGEMENT ON THURSDAY AT 8:30 AM. YOU ARE INVITED; WE WANT TO RECRUIT YOU.