The Human Dimension of the Asian Financial Crisis

Uncertainties in Southeast Asia have compounded current concerns about the performance of the Japanese economy, in turn contributing to global anxiety about trade dislocation and international growth levels.

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A Summary of Discussion at the Jakarta Experts' Meeting

Since July 1997, Southeast Asia has been in profound turmoil as currency crises have precipitated economic and political instability. The crisis has also brought with it implications beyond the most affected economies (in particular, the Republic of Korea, Thailand, Malaysia, the Philippines and Indonesia). The knock-on effects on international trade have extended into other APEC and non-APEC economies as markets for both exports and imports have faltered. Uncertainties in Southeast Asia have compounded current concerns about the performance of the Japanese economy, in turn contributing to global anxiety about trade dislocation and international growth levels. Strenuous efforts have been made by international financial institutions, especially the IMF, to bring some financial orthodoxy to bear on the most affected economies, provoking a complex debate about the appropriateness of policy responses to the crisis. This debate has been conducted at various levels, including the technical mix of measures for the creation of financial stability, the timing of such measures, their appropriateness in terms of traditional financial and business practices in the most affected economies, and, importantly, their impact on social and political processes.[1]

In many ways, the crisis has been all the more shocking because of the recent performance of the most affected economies. They have experienced annual growth rates of 6 per cent-plus for many years. They have seen export markets grow impressively. Foreign capital has flowed into manufacturing, the financial sector and into property. Labour forces have been transformed. Adaptation to technological advances has proceeded apace. A perception grew that the economic success of the "tiger" economies of Asia was in some way impregnable. The current crisis is felt all the more severely because of that seemingly flawed impregnability.

However, despite the image of permanent economic success in the high-performing Asian economies, some observers anticipated the crisis. For example, in a September 1996 article, an argument advanced the prospect that the 1996 flurries against the currencies of Malaysia, Thailand and Indonesia presaged a Mexico-style "meltdown" (the IMF's Morris Goldstein, reviewed in *The New Zealand Herald*, September 2, 1996, p. B5). Based on the 1994 Mexican crisis, Goldstein identified seven danger signals, which supported this concern. They were:

- a mismatch between short-term debt and foreign reserves
- a big current account deficit
- increased consumption rather than investment
- budget deficits
- dependence on foreign capital inflows
- overvalued exchange rates, and
- rapid monetary growth.

Goldstein went on to argue that Thailand was the most vulnerable of the Asian economies in terms of these signals, with Malaysia and Indonesia close behind. At that stage, the November 1997 collapse of the South Korean won was not widely envisaged. Goldstein was shown to be prophetic by the events of 1997.

The Crisis: A Brief Overview[2]

The immediate trigger of the crisis was the devaluation of the Thai baht in July 1997. As we note in the discussion that follows of the four case studies (Malaysia, the Philippines, Indonesia and Thailand), the striking impact of the Thai devaluation was its replication in other regional

1 The web page at http://www.stern.nyu.edu/%7Enroubini/asia/AsiaHomepage.html is a good source of material on the crisis and its associated technical debates.

2 This section is drawn in part from the overview in *The Social Impact of the Asian Financial Crisis*, (ILO: Bangkok, April 1998), pp. 1-11.

economies.[3] Currencies were devalued dramatically (in Malaysia, Indonesia, Korea, the Philippines and Thailand by around 35 per cent). The currency crisis triggered dramatic collapses in regional stock markets, losing between 40 and 55 per cent of value in these same economies. A key factor underpinning both currency and stock market collapses was the reversal in foreign capital flows. In the most affected economies, net private inflows fell from US$93 billion to negative US$12 billion in the period from the end of 1996 to the end of 1997, estimated to represent a reversal in GDP of 11 per cent.

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Institutionally, the regional banking system was shown to be unable to cope with the crisis. A high level of dependence on unhedged short-term loans was a significant factor, particularly in Thailand. Corporates were vulnerable to similar lending arrangements, especially in Indonesia and Korea. Corporates also maintained high debt-to-equity ratios, which exacerbated the impact of their borrowing regime. As interest rates rose in response to the currency crisis, even viable corporates became vulnerable to the financial and institutional consequences of the crisis. Confidence in trade relationships and their instruments fell and exporting firms were unable to benefit from the impact of devalued currencies. As a result, the GDP in 1997 fell away, particularly in Thailand, and is projected to suffer dramatically across the region in 1998, with something of a recovery proposed for 1999 (see Table 1).

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The impact of the crisis has not been evenly spread across the region. For example, Thailand, Indonesia and Korea have been particularly badly hit; Malaysia and the Philippines, both with a lower exposure to short-term overseas debt, have experienced less severe impacts.

The ILO points to the extended and unresolved debate about the origins of the crisis. It is this lack of a resolution that makes the development of an appropriate strategy difficult in the midst of the crisis. For the ILO, the actions of the international financial market have played a part in creating the conditions for the crisis, in particular in terms of its lending profile over preceding years and its over-reaction to the crisis once in train. Domestic imperfections are also highlighted, including the regulation of domestic financial structures in a period of financial liberalization, the unquestioned commitment by governments to an externally funded, high-growth strategy, the mechanisms put in place for handling the massive capital inflows (particularly exchange rate and interest rate policies) and the impact of "crony capitalism."

Domestic imperfections are also highlighted, including the regulation of domestic financial structures in a period of financial liberalization.

Table 1

Real GDP Growth
(per cent)

	1996	1997*	1998*	1999*
Thailand	6.4	0.1	–3.0	1.8
Indonesia	8.0	4.6	–0.1	2.6
Korea	7.1	5.8	0.6	4.4
Malaysia	8.6	7.4	3.4	5.1
Philippines	5.7	4.9	3.0	3.6

* These figures represent the average of IMF, *The Economist* International Business Unit and Union Bank of Switzerland estimates.
Source: adapted from ILO, *The Social Impact of the Asian Financial Crisis*, p. 2.

The Social Impacts of the Crisis

The ILO has provided a succinct and telling overview of the social impacts of the crisis (ILO, *The Social Impact of the Asian Financial Crisis*, pp. 12-30). Social impacts derive from the sudden reversal in economic fortunes from a situation in which, generally,

3 This replication has been interpreted in a number of ways. Some commentaries have invoked the idea of contagion; others focus on a set of individual cases in which economic fundamentals were ignored or unstable. In the latter case, some mechanism by which the events in Thailand were transmitted across regional boundaries is still required.

This reversal is taking place in economies with minimal social safety nets.

rates of job creation, in jobs with reasonable wages, exceeded the rates of growth in the labour force to a situation marked by retrenchments, reduced rates of new hiring, rising unemployment and underemployment, and the prospect of declining real wage levels. This reversal is taking place in economies with minimal social safety nets, and widespread expectations about growth, which can no longer be met in the short term.

The crisis affects women workers in particular ways. Not only do they face reduced opportunities in formal employment as a result of the crisis, but they also face difficulties because of the downstream effects on the informal sector and on family structures. They may also be disadvantaged in terms of access to relief measures and their impact on decision making in response to the crisis. Migrant labour also faces particular difficulties, as retrenchment and downturn may lead governments to consider substituting immigrant labour with indigenous labour. Moreover, this may take place in contexts where the export of labour is seen as a potential answer to job loss and unemployment. In the April seminar in Jakarta, it was also suggested that older, male workers will face significant consequences as a result of crisis-driven restructuring. In particular, they will experience major problems in terms of finding new jobs, and subsequently may lack the ability to cope with the social consequences of unemployment.