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COPING WITH CONTAGION: EUROPE AND THE ASIAN ECONOMIC CRISIS

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Coping with Contagion

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Exhibiting his usual penchant for affixing interesting titles to his budget speeches, in February this year the Hong Kong Financial Secretary Sir Donald Tsang introduced his annual budget by talking about 'riding out the storm'. The storm he was referring to was the series of financial crises which have swept the Asian Pacific region since the middle of 1997. With three regional states having to appeal on bended knee to the International Monetary Fund (IMF) for financial infusions and all the other regional states affected to some degree or other, the bloom seems to have gone off the Asian Pacific economy.

In Europe, the series of Asian Pacific crises has been met with differing reactions, but overall there have been two dominant tendencies: either to treat it as 'a fire on a distant shore', to borrow a phrase much used by Japanese, and to minimise the extent to which it will actually impact on the realities of European trade, investment and financial flows, or to express quiet satisfaction that the previously increasingly confident, even cocky, Asians have finally got their come-uppance. Neither of these reactions, however, pays full due to the importance for Europe of this dramatic change in the political economy of the Asian Pacific region.

The Asian Financial Contagion:

Since the middle of 1997 a series of financial and economic problems have swept across the Asian Pacific region. In the view of Singapore prime minister Goh Chok Tong these constitute the region's 'worst crisis and biggest test since World War II' (Korea Herald, 14 January 1998). Malaysian prime minister Dr Mahathir Mohamad
has lamented that 'the economic turmoil ....reduced the tigers to whimpering kittens' and argued that 'the massive damage to their economies would take decades to be restored' (Straits Times, 3 March 1998). The Singaporean newspaper, the Straits Times, actually started in March 1998 a separate website entitled 'Asia in Crisis' to carry regional stories on the developing situation.

First Thailand, then Indonesia and finally South Korea have all had to go to the IMF, other regional and international financial institutions and to key major economic powers including the European states for financial assistance to tide them over mounting debt problems. Malaysia and the Philippines have avoided direct appeal to the IMF, but nonetheless have suffered a rocky period and have been forced to introduce their own austerity measures, albeit not as severe ones as the IMF-imposed ones in Thailand, Indonesia and South Korea. By January 1998 the Malaysian ringgit, the Philippine peso, the Thai baht, the Indonesian rupiah, and the Korean won had all fallen in value by between 40-60% against the US dollar since the beginning of July 1997 (see Table 1). Malaysian prime minister Dr Mahathir claimed that the currency depreciations had wiped about $200 billion off the wealth of the Southeast Asian nations (South China Morning Post, 16 November 1997).

Over the same July-December 1997 period the stock-market indices of those five economies also dropped by around half their value. One estimate has suggested that, despite some partial recovery in stock market prices in early 1998, in total some $600 billion, the equivalent of two-fifths of the region's gross domestic product (GDP), had been wiped off stockmarket values across the whole region (Economist, 7 March 1998). The Thai, Indonesian and South Korean economies are expected to suffer either close to zero or even negative growth in 1998. Singapore, Hong Kong, China and Taiwan have resisted these financial pressures more successfully, but because
they are closely tied into the Asia Pacific economy they have not been unaffected by what has been happening in other parts of the region. The Singapore stock market, for example, continued to shudder in January-February 1998 as the Indonesians debated and argued with the IMF over the merits of setting up a currency board to peg the rupiah to the US dollar. With the exception of China, which is expected to achieve around 8% growth (but still below its recent record), all these economies are expected to be achieving under 5% growth in 1998. The smaller regional economies, such as the Indochinese states and Burma, have been relatively unaffected because of their limited involvement in the regional and global financial markets but, given that Thailand in particular and other Southeast Asian economies to a lesser extent have been important investors in their economies, they are beginning to suffer some knock-on effect from the Thai crisis.

Views differ as to the underlying and proximate causes of these financial crises and clearly the situation is not exactly the same in each country. Conspiracy theorists have had a field day: some latching on to the speculative activities of international financiers such as the now notorious George Soros, others trying to lay the blame on actions by major economic powers such as the Chinese devaluation of the yuan in 1994 or the US' desire to open Asian markets to US goods and services. However attractive these theories might seem, they do not provide the real answer. The immediate cause can be put down to foreign over-borrowing by Asian Pacific banks, corporations and individuals on a short-term basis. Banks across the region have found themselves sitting on mountains of non-performing loans. But there were a number of structural defects which contributed to the severity of the crisis (Tan 1998): the use of political rather than commercial criteria in the allocation of loans (especially in Thailand and Indonesia), over-expansion of manufacturing capacity (South Korea), poor supervision of financial institutions and systems (most of those countries suffering
now), and a penchant for mega-projects at above-market prices (Malaysia and Indonesia). Unlike earlier crises in Latin America, the Asian Pacific region is not so worried about government over-spending and sovereign debt; the problem is more with private and short-term debt.

Just as the earlier economic boom and economic 'miracle' was not universally and consistently in evidence throughout the Asian Pacific region, so it can also be said that the current economic turmoil in certain countries does not mean that the whole region without exception is in deep crisis. However, the speed and extent to which the turmoil spread was a surprise to almost everyone within and outside the region, including, it has to be said, the IMF itself, which only a few months before had been praising the sound macroeconomic policies of countries such as Thailand and South Korea (International Herald Tribune 19 December 1997). In the early weeks of the crisis there was a tendency to underplay the extent of the problem. Even US president Bill Clinton, attending the Asian Pacific Economic Cooperation (APEC) summit in Vancouver in November 1997, described the problems as just 'a few little glitches in the road' to prosperity (Asian Wall Street Journal, 25 November 1997), a view he was soon forced to revise. By January 1998 his administration felt the need not only to show political support for the battered Asian economies but also to persuade some countries, most notably Indonesia, that taking the IMF-prescribed medicine was essential to a healthy recovery.

But what are the prospects of recovery and how long will it take? Getting back to full health, in terms of growth rates reminiscent of the mid-1990s, will certainly take several years. The Economist believes that for many of the regional economies GDP growth will 'remain weak until 2000 at the earliest' (Economist, 7 March 1998). In part, the future depends on whether the most affected economies are prepared to take the
IMF medicine and whether in fact the IMF has prescribed the right medicine in the first
place, since IMF officials initially approached the Asian crisis heavily influenced by their
past experience with Latin America and have themselves been going through a
learning process as the contagion spread across the Asian Pacific region. But in terms
of restoring regional and international confidence, a crucial psychological factor in the
economic recovery scenario, to be seen to be undertaking the IMF programme is
nonetheless important. In that sense, both Thailand and South Korea are buckling
down to the task at hand, whereas Indonesia is seen as still being recalcitrant and
consequently continuing to suffer on the foreign exchange and stock markets.

In part also, however, the prospects of an early recovery for the Asian Pacific
regional economy depend on two major regional economies which are both too
preoccupied with their own problems to provide real help at the moment. Firstly, Japan,
which has been labouring under its own financial problems coupled with a prolonged
recession and, unfortunately, has not been able to provide the economic leadership
and market stimulation that many other Asia Pacific countries have hoped for. Although
prime minister Hashimoto Ryutaro returned from a December 1997 summit with the
leaders of ASEAN (the Association of Southeast Asian Nations) with a much better
appreciation of how the crises around the region would seriously affect Japan (Nikkei
Weekly, 22 December 1997), the series of stimulus packages released through late
1997-early 1998 proved only to be damp squibs. Secondly, China, which has appeared
not only as the only regional market with reasonable business prospects and
reasonable growth expectations in the immediate future but also another economy
which would adversely affect other economies' recovery should it decide, in order to
retain competitiveness, to devalue the yuan and start another round of competitive
devaluations. However, pronouncements by the top leadership in early 1998 ruled out
yuan devaluation as an option at least for the short term. China contributed to the
international rescue package for Thailand, but did not directly assist either Indonesia or South Korea. President Jiang Zemin’s benevolent disposition at the December 1997 ASEAN summit was not one which, given China’s mounting internal economic problems (particularly the question of reforming the bankrupt state-owned sector), could easily be translated into solid assistance for the rest of the region.

Looking at Japan’s postwar economic record, especially since the first oil shock brought the first actual and psychological hiccup in an apparently unending economic growth pattern, it is clear that Japan has been able to treat economic setbacks as a form of ‘blessing in disguise’ to restructure and come back stronger than before (though admittedly the current prolonged recession suggest that it is not responding now as agily as in the past). This characteristic has also been exhibited by South Korea in the early 1980s and Singapore in the mid-1980s. Therefore, with the possible exception of Indonesia, there does seem every prospect that the region can recover and once again, now doubt even more competitive as a result on the enforced reforms, bounce back as a dynamic economic area in the medium term. But before everything returns to ‘business as usual’ there will be much discomfort and disruption not just for the states of the region but also for their external trading partners. Confidence once lost is not so easily regained.

The spread of the financial turmoil across the Asia Pacific region was indeed evidence of the extent to which the regional economies are now closely interconnected, in way that conceivably even a decade ago was not so evident. But as the Bank for International Settlements noted in its March 1998 quarterly review of financial markets, the crisis in the Asian Pacific region has also ‘served as a painful reminder that the interconnections between [global] markets are becoming increasingly complex’ (BIS 1998). This means that Europe too has been affected by the Asian troubles.
Impact on Europe:

At the early stages of the financial crisis the Europeans, like the Clinton administration, tended to underestimate the extent to which it was developing. Most European governments and companies have consistently lagged behind events in appreciating the degree to which the Asian problems might impact on their own economies. There were certainly many Europeans who could not avoid a certain degree of relief and indeed grim satisfaction, given past Asian pronouncements on the superiority of the Asian way of doing things, that all was not well with the Asian 'miracle' and that the Asians appeared human after all (Higgott 1998 p.4). The South Korean crisis in November was the one which seemed to finally wake up many Europeans and, in fact, it was the four European members of the G-7 group which were first, ahead of the Japanese and the Americans, in offering to help to South Korea (Interview, European Delegation, Seoul, November 1997). European Commission officials stepped up their surveillance of the Asian financial crisis and even began to consider 'worst-case scenarios' (Financial Times, 29 January 1998).

Yet despite the magnitude of the Korean problem and increasing signs of socio-political disorder in Indonesia, even in January 1998 European Commission president Jacques Santer argued that the direct effect on the European economies of the Asian Pacific economic turmoil would be 'slight' and that he saw no need to revise downwards growth projections for the European Union (EU) for 1998 as a result (Nihon Keizai Shimbun, 12 January 1998). Later the same month, the EU's monetary affairs commissioner, Yves-Thibault de Silguy, also argued that the Asian crisis would have 'only a marginal impact on growth in Europe' (Financial Times, 29 January 1998).
This kind of approach is clearly over-optimistic. Indeed, some European leaders, such as Tony Blair, the British prime minister, have recognised this; when meeting with Japanese prime minister Hashimoto in mid-January he agreed that the Asian financial crises would have "a great influence on the global economy" (Nihon Keizai Shimbun, 13 January 1998). Continued problems with Indonesia's non-compliance with the IMF programme could yet, as one British minister warned his European and Asian counterparts, send it into 'almost uncharted waters' and conceivably set off a second wave of lack of confidence in the region (Straits Times, 16 March 1998).

In general terms, the global economy has already been pushed into a slowdown which is likely to cut one percentage point of global growth in 1998, although available growth figures have yet to fully reflect the impact of the Asian troubles. Instability in currency markets in early 1998 make predictions difficult, but there a number of ways in which the Asian problems will specifically impact on Europe and European business with the Asia Pacific.

(1) Trade:

The Asian Pacific countries collectively have become important trade partners of the EU. The development of the single market in Europe has helped to push the already high degree of intra-regional trade even higher, so that by 1996 around 61% of the EU's total trade was amongst its own member countries. But amongst the EU’s external trade partners the Asian Pacific countries have slowly but steadily grown in importance, although Japan is still by far the largest trading partner, accounting for nearly one third of the EU-Asian Pacific trade. According to IMF figures, in 1990 for the first time EU (then technically still the European Community) trade with the 15 main Asian Pacific countries exceeded the EU's main trade with the United States. By 1995 EU-Asian Pacific trade was more than 30% larger than EU-US trade. In 1996 (the most
recent year for which full IMF figures are available), EU exports to the region totalled $169 billion (8.3% of total EU exports) and imports totalled $207 billion (10.6% of total imports), giving an overall deficit for the Europeans of $38 billion. This deficit seems destined to widen noticeably.

Certainly, European exports to the Asian Pacific will be dampened by the series of crises. With the most-affected Asian Pacific economies embarking on austerity measures which include reducing or discouraging imports of 'luxury' or non-essential items, especially consumer goods, and cancelling or re-negotiating some specific government procurement contracts already agreed. The Europeans had already been complaining prior to the crisis about an unofficial 'frugality' campaign in South Korea which was seen as discriminating against foreign, including European, goods in the name of reducing trade imbalances. But, the Koreans are not alone any more; for example, in early March the British felt moved to protest officially to the Thai ministry of public health over a policy of encouraging Thai hospitals to buy locally-made drugs rather than imported British ones (Bangkok Post, 10 March 1998).

Although the five most affected Asia Pacific countries have seen their currencies depreciate rapidly against the US dollar, they have also fallen against the major European currencies and in most cases indeed even more drastically than against the US dollar (see Table 1), so those goods which are still being imported from Europe are becoming more expensive in local currency terms. German exporters are probably in the best position of the major European exporters as the deutschmark also declined against the dollar during 1997 giving them a competitive price advantage (International Herald Tribune, 16 December 1997). However, even in those Asian Pacific economies whose currency is either pegged to the dollar or not depreciating so significantly, Asian consumers are likely to be both more cautious and, in some cases,
more interested in rival consumer products coming out of the suffering Asian economies which are now comparatively cheaper. European exporters will find a decreasing demand for many of their products, especially consumer goods. France, for example, has reported that its monthly figures for exports to the Asian Pacific region excluding Japan in December 1997 had dropped by 40% from a peak in mid-1997 (Nihon Keizai Shimbun, 25 February 1998).

At the same time, imports into Europe from these same Asian Pacific countries will increase as their depreciating currencies have made their products much cheaper and therefore more competitive. For many of these suffering economies, increased exporting seems to be one of the few solutions easily available. Although, of course, the financial crunch in these exporting countries means that some companies will find it more difficult to get short-term loans or credit from banks particularly when they need to cover the rising costs of imported raw materials and/or components that are a key element of their final products, increased exporting as a policy seems certain. One Korean economic research institute has forecast that South Korean exports to the EU would rise 17% in 1998, more than double the expected overall growth in Korean exports (Korea Herald, 17 January 1998). The combination of increased exports from these Asian economies coupled with decreasing export opportunities for Europeans will inevitably lead to a deterioration of Europe's bilateral trade imbalances with these Asian countries. For example, according to French statistics, with a drop in its exports and an increase in its imports in December 1997 France recorded its largest monthly deficit for three years in trade with 10 Asian Pacific countries apart from Japan (Nihon Keizai Shimbun, 25 February 1998). If the past record of European reaction to surges in Asian Pacific exports is repeated - and that is likely to be the case where unemployment remains a serious political problem, especially in France and Germany - then protectionist pressures would again rise within the EU.
(2) Investment:

Like the trade situation, the environment for foreign direct investment (FDI) is changing, although the picture here is more mixed. Overall, there is likely to be a decline in new European FDI into the Asia Pacific region. Some European companies, especially those operating in the financial sector, are already undergoing consolidation and even withdrawal in a few cases. In the manufacturing or resource-exploiting sectors, cost-cutting measures are likely to be the order of the day, especially where the products are destined mainly for the local market or for other regional countries with devalued currencies. But exporting from countries with devalued currencies to other economies in the region with non-devalued currencies (with China the key target) could be boosted. For example, Swiss-Swedish engineering company ABB is shedding contract workers and cancelling bonuses for its executives at its Thai factories, but is gearing its plants up to actually expand production and develop a new regional export strategy (Far Eastern Economic Review, 5 February 1998).

A growing type of investment as a result of the economic crises, however, is likely to be debt-to-equity conversions and merger and acquisition activity. This may become particularly visible in countries such as South Korea, which under IMF supervision is having to dramatically increase the limits allowed to foreign companies in taking ownership of Korean companies and to liberalise further its regulations on inward FDI. Even in Hong Kong, relatively unaffected by the regional financial instability, Europeans have found opportunities. French and Spanish banking groups moved in early 1998 to take over parts of the operations of one of Hong Kong's largest financial groups, Peregrine, when it went bankrupt through over-exposure in Indonesia.
In addition, still looking at FDI, there is likely to be a fall in Asia Pacific FDI into Europe, particularly from South Korea but also from Japan and the other newly-industrializing economies (NIEs) too. Inward investment into Europe from Japan, since the mid-1980s, and the Asian NIEs, primarily since the early 1990s, has been increasing, even though it is still a comparatively small share of total EU inward investment. In the 1990-95 period, after the Japanese financial bubble burst and outward investment slowed, the EU took an average of $7.2 billion per year from Japan and $1.1 billion from the other Asian countries (UNCTAD 1996); together they represented less than 10% of the investment inflows in those years. Nonetheless, for certain EU member countries, especially Britain which now holds around two-fifths of the EU’s stock of Asian inward investment, cancellations or cutbacks could have important employment effects. As a portent of what is to come, Daewoo announced early in 1998 that it was putting on hold its plans to start a cathode-ray tube plant in eastern France and Hyundai decided to suspend its plans for the next phase of expansion to its Scottish semi-conductor plant (Far Eastern Economic Review, 5 February 1998). Some of the small and medium-sized companies which have followed the bigger Japanese and Korean companies into Europe as suppliers are likely to withdraw completely.

(3) Bank loans:

European banks have found themselves heavily exposed to some of the countries most at risk and have been forced to undertake serious discussions with both Asian governments and companies to set up private-sector rescue packages to sort out short-term debt repayment problems. On the eve of the crisis, in mid-1997, for example, German banks were exposed in South Korea to the tune of $10.6 billion, French banks $10.1 billion and British banks $6.1 billion. After crisis talks with the South Korean central bank governor in early 1998, they agreed to work out a roll-over
solution which avoided a formal debt rescheduling (Sunday Morning Post, 11 January 1998). According to Banque Paribas estimates, European banks were exposed to the tune of at least $15.5 billion in Thailand ; after talks between Thai prime minister Chuan Leekpai and German chancellor Helmut Kohl in early February, most of the European banks seemed prepared to enter into rollover arrangements for Thai corporate debt (Hongkong Standard, 2 February 1998).

This picture of heavy European financial exposure is repeated across the region. One German bank alone, Deutsche Bank, is estimated to have about $16 billion in loans outstanding spread across 8 Asia Pacific countries (Asian Wall Street Journal, 22 January 1998). Overall, according to figures released by the Bank of International Settlements, as of June 1997 European banks held $365 billion in loans outstanding to Asian banks and companies, more than the total of the American banks ($275 billion) and the Japanese banks ($45 billion) combined (Far Eastern Economic Review, 12 February 1998). Worries about Asian Pacific regional financial stability, especially in Indonesia, are certain to continue for the European financial community. While no European banks are likely to be bankrupted by their Asian commitments, their earnings and profits will undoubtedly be hit. Deutsche Bank, for example, suffered a 57% fall in its net profits during 1997 primarily because of its exposure in Asia (South China Morning Post, 19 February 1998).

(4) Flows of people

Flows of people will be reduced. Those European states which benefit from the ubiquitous Japanese, Korean and other Asian tourists will undoubtedly notice a drop-off in visitors. European airlines connected to Asia will also suffer in the short run ; the prospect of cheaper holidays in some parts of the Asian Pacific region for Europeans is unlikely to provide sufficient compensation to the airlines for the drop-off in Asian
travellers to Europe. British Airways, for example, has announced that it will be suspending its flights to Seoul from March because of the slump in demand. Students and young people, a fruitful seed for future inter-regional linkages, coming from the worst-affected Asian countries to study in Europe may also be reduced in number. The Malaysian government, for example, has already begun to set up new credit-transfer procedures to encourage its students in financial difficulties while studying in Europe to return home to local private universities.

(5) European monetary union (EMU)

The Asian financial crises may also indirectly have some impact on the EU's own progress towards EMU and the creation of the new euro currency unit. There is as yet no sign of a delay to the deadlines for moving towards the EMU, which is anyway far more likely to be affected by fiscal and monetary policies within individual EU countries than by Asian developments. Nonetheless, given the heightened Asian sensitivity to currency-related issues, the Europeans will have to try to reassure the Asians that the single currency would not be manipulated to protect European jobs from cheap Asian imports coming out of the affected countries.

However, the emergence of the euro from January 1999 could have more of an impact on Euro-Asia trade transactions than might have been the case if no financial crisis had occurred. At the moment, although the Germans do denominate much of their Asian trade in deutschmarks, in general the US dollar is the dominant currency in Euro-Asian trade. That could change after 1999. As Philip Bowring has argued, a single currency in Europe and continued exchange rate volatility in Asia suggest that a diversification of trading currencies away from the mighty dollar would be 'opportune' for the Asians (Bowring 1998). The euro could be part of the answer for Asia.
Political repercussions:

In the post-Cold War world, economics cannot easily be separated from politics, or, for that matter, from national and regional security. To some extent political stability in the countries of the Asian Pacific region has been associated with economic development, and political leadership has been legitimized by the success achieved in this respect. The inability not only to sustain economic development programmes and the related growth in incomes, but also, in several of the regional states, to cope with upsurges in unemployment and bankruptcies, could lead to socio-political strains and possibly instability. Thailand has seen a change of government in November 1997 as a result of the economic collapse and the success of the opposition candidate in the December 1997 South Korean presidential elections (heralding the first ever victory for the opposition in a presidential election) was at least in part due to the economic crisis there. But, in both cases, the social fabric seems to have survived, although the worst of the pain, particularly in the South Korean case, is yet to come. Indonesia, however, has not only seen no political change at the very top, for president Suharto was re-elected by a hand-picked electoral college in March 1998 for a record seventh five-year term, but has been experiencing the most obvious signs of socio-political unrest. Anti-Suharto student demonstrations, anti-Chinese riots, runs on banks and foodstores, and threats from the military to use force if necessary to restore order suggest a nation under siege.

References to their support for security and stability in the Asian Pacific region have long been part of the rhetoric of European political leaders and officials. In practical terms too that means that the Europeans cannot but be concerned about the socio-political repercussions of the economic downturns, especially in the case of Indonesia, both for their direct impact on European businesses' ability to safely and
effectively carry out their trading and investment activities and for the more indirect impact on national and regional stability. Floods of poor, even starving, Indonesians setting sail for Malaysia and Singapore or taking up piracy in the Straits of Malacca can affect not just the neighbouring nations but European interests in those countries too.

More difficult to judge is what the Europeans can do to help minimise this socio-political fall-out. In the post-Cold War world, the Asians have become if anything more sensitive to what are perceived as attempts by the West, which means the Europeans as much as the Americans, to intervene in the internal affairs of individual countries. Clashes over human rights have occurred on an increasingly regular basis at meetings between Europeans and Asians in the 1990s, especially as individual EU governments as well as the European Commission began to link human rights to trade and economic assistance policies. As a result, there has been a tendency over the past year or so for the Europeans, for the sake of maintaining constructive relations, to generally back away slightly from pushing issues such as democracy and human rights. China is an obvious beneficiary of this policy, while Burma remains the exception to the rule as the one country that is still high on the European 'hit list'. This means that the Europeans have tended also to avoid directly linking political openness and economic transparency in their recent dealings with the Indonesian government. The hope is that by urging economic reform - and the Europeans have, for example, been strongly urging Indonesia to take the IMF medicine and give up the currency board idea (see the comments by the British special envoy when he met Suharto, Nihon Keizai Shimbun, 6 March 1998) - the realisation that a more open, i.e. democratic, political system could also help may well follow. Quiet diplomacy rather than megaphone diplomacy has been, and should continue to be, the hallmark of European attempts to encourage greater political stability.
A more nebulous result of the crises could be that the European image in Asia may also be enhanced if the Europeans act in a responsive manner. With the end of formal colonialism (though not necessarily of all the cultural, political, socio-economic and psychological legacies of that experience) and subsequently the Europeans' tendency to turn in on themselves for long periods, the Europeans have often seemed to be out of the picture in Asia and certainly to be a very weak counter-balance to US commercial and political influence in the region. However, the always-present Asian Pacific ambivalence about the Americans has increased as a result of the events since mid-1997. The United States was slow to contribute directly to solving the regional crises, tending to limit its early role to endorsing the approach of the IMF, in which admittedly the United States has an extremely influential voice. Although initiatives in late 1997 to create some form of Asian regional emergency fund as an alternative to the IMF have so far fallen by the wayside and the Asian Pacific nations have had to fall back on approving the US approach of controlled funding through the IMF, there has been growing resentment of the American role. The Chinese media, for example, denounced US intervention in the financial crises as a cynical plan for 'forcing East Asia into submission [and] promoting the US economic and political model' (South China Morning Post, 7 January 1998). A new best-seller in South Korea by a Seoul National University sociology professor describes 'Korea's surrender to the invincible armada of US Wall Street capitalism' (Korea Herald, 3 March 1998).

While a few Asian Pacific politicians have been scathing about the West and its financiers in general, thereby including by implication the Europeans, on the whole the Europeans have been subject to less criticism. For example, even though cumulatively the European states contribute a larger share financially (totally 30%) to the IMF than
the Americans, it has been the United States which has been cast in the villainous role as the 'controller' of the IMF. While admittedly playing a lower key role than that of the United States the Europeans have therefore also played a less controversial one. By appearing to be constructive rather than gloating or dismissive, the Europeans can prove that they can be a useful friend for those Asian states in need.

A Test for ASEM:

The APEC summit in Vancouver in November 1997, despite coming in the midst of the Asian financial crises and indeed exactly as the South Korean collapse was becoming so clear, failed to add anything substantial to the IMF-led measures of relief. It seemed to have little to offer when faced with the first real test since its establishment eight years earlier. Early April 1998 will provide a test in turn for the much newer inter-regional organisation, the Euro-Asia summit or ASEM (the Asia-Europe Meeting as it is formally known), which has set off with less fanfare and lower expectations than APEC, but which does now have a better opportunity, as the dust begins to settle slightly on the Asian crises, to consider at its London meeting measures and mechanisms which can help to reduce the damage that might occur from any repetition of these crises.

The political initiative for the ASEM process came from the Singaporeans, but it also reflected wider ASEAN concerns to balance their relationship with the oft-times over-bearing United States by establishing links elsewhere. The first ASEM was held in Bangkok in March 1996; Europe was represented by the 15 member states of the EU and Asia by the existing seven members of ASEAN plus Japan, China and South Korea, a grouping which in composition was very close to that much earlier but previously un successfully advocated by Malaysian prime minister Dr Mahathir under the rubric of an East Asian Economic Caucus (EAEC). The ASEM proposal appealed to
the Europeans because it coincided with a general review already under way of European policies towards Asia based on a growing realisation of the economic importance of the Asian Pacific region and the weakness of the European involvement in that region (Camroux and Lechervy 1996 p. 444). This shift in European perceptions was most clearly shown in the European Commission's own policy document drafted in mid-1994 which strongly argued the case for the EU to accord a higher priority to Asia and to adopt pro-active and better coordinated strategies towards the region (Commission Communication 1994).

The model of APEC was clearly on the minds of many participants. The Italian prime minister Lamberto Dini, the president of the European Council, hoped that ASEM would 'one day be on a par with the tried and tested links' of APEC, but as the EU vice-president Brittan made clear 'in paralleling the APEC process, we are not aping the APEC process' (Asian Wall Street Journal, 4 March 1996). This means that while both sides were prepared to follow APEC in focusing predominantly on economic cooperation issues, there was no intention to mimic APEC either in its specific goals and target dates for trade and investment liberalisation or in its slow progress towards institutionalisation. Reference instead was made to the WTO and its implementation procedures; the ASEM process should 'complement and reinforce efforts to strengthen the open and rules-based trading system embodied in the WTO' (Chairman's Statement 1996). No ASEM Secretariat was suggested; indeed the Europeans argued that ASEM should not become too bureaucratic or rigid. Summit meetings are to be held every two years, not every year as in the case of APEC. There is also one other clear difference between APEC and ASEM in that, from the very beginning, the political dialogue has been an integral part of the ASEM process, whereas despite the efforts by some countries such as the United States and Australia political issues have
remained largely outside the scope of APEC meetings, even at the annual summit gatherings.

The ASEM-related activity since the 1996 Bangkok summit has clearly been designed to ensure that that particular meeting did not end as a one-off jamboree in the sun. The Bangkok meeting has been criticised for adopting a 'laundry list strategy', allowing each country to put forward its favourite project, with no sense of priority (Segal 1997 p. 134). The difficult part, therefore, is to set priorities and to translate all these various initiatives and proposals into practical results. The hosts of ASEM 2, the British, in the months beforehand certainly tried to emphasize the need for 'good, solid and practical ideas' (Bangkok Post, 10 February 1998). The very economic crises which have hit the Asia Pacific region may well act as a factor in helping to establish priorities since, from the Asian perspective, not everything is as easily achievable as once seemed possible. Two plans which had been under discussion prior to the financial crises are still to be put forward to the London ASEM: an investment promotion action plan (which will include using the Internet to collate investment possibilities) and a trade facilitation action plan. Despite their rather unexciting names they are intended to boost trade and investment links in the longer term by measures such as simplifying customs procedures and improving intellectual property rights. While these two plans are set to go ahead at the London summit, it is likely that their character will be altered by the need to respond to the Asian financial crisis.

As European Commission vice-president Sir Leon Brittan has argued, Europe has learnt much about market opening and prudential financial supervision from its own process of creating the single market as well as its own past problems with financial collapses (such as Bank of Credit and Commerce International and Barings) (Brittan 1998). Some practical steps, such as the technical assistance which has already been
extended by the Bank of England to the Thai authorities on the management of reserves (Bangkok Post, 10 February 1998), could therefore be extended to other countries in the region, although specific programmes should be tailored for individual countries.

The British government, in its capacity as the EU presidency, has also begun to float the idea of an ASEM Trust Fund, which would be designed to ease the impact of social change, poverty and labour market reforms and would be managed by the World Bank's special financial operation unit. Britain has already promised $3 million as seed-money to start off the fund, but is hoping to persuade its EU partners to also contribute (Bangkok Post, 25 February 1998). Steps such as the ASEM Trust Fund and technical assistance programmes are both practical and distinctive steps that the Europeans can take to demonstrate their commitment to the Asia Pacific.

Richard Higgott has argued that the net effect of the Asian financial crisis will be to increase interest in East Asian, as opposed to Pacific-wide, regionalism (Higgott 1998 p. 6). Certainly, Asian disillusionment with the Vancouver APEC meeting's results, ambivalence about the American role in the Asian financial crisis, and preliminary intra-regional discussions in early 1998 about trading in the Singapore dollar, instead of the US dollar, amongst ASEAN economies as the first step to what might lead to an 'Asian currency' suggest that the Asians may well be turning in on themselves or at least trying to redefine themselves in contra-distinction to the Americans. However, it is still early days - and Singaporean reluctance to allow its currency to become a regional one suggests that there are serious limits to such regionalisation. Nonetheless, if East Asian regional identity or consciousness does become strengthened then ASEM which posits, or at least up until now, has posited
the EAEC membership as its Asian component will be well-suited to accomplishing a
region-to-region dialogue with Europe which is consistent with Asian aspirations.

A new phase in Euro-Asian relations:

Whether or not Marco Polo did actually travel around China, European interest in and contacts with Asia certainly date back many centuries. In broad historical terms, a number of different periods of Europe-Asia interaction can be demarcated, although inevitably dating can only loosely be applied given the range of countries involved and the differing dynamics in their individual interactions with the other region. The first period would cover the initial contacts in ancient times through to the beginning of serious European colonization in the early/mid-nineteenth century. It was characterised by intermittent and sometimes accidental cultural cross-fertilisation and trade flows, with on balance more going from Asia to Europe than vice versa. The second period, from the mid-nineteenth century until World War II, was the period of formal European imperialism and colonization throughout much of the Asia Pacific region. This was essentially an exploitative and dominant phase for the Europeans.

The third period began with the Japanese attack on European possessions in the Asian Pacific region, which first laid bare the European weaknesses, and covered the subsequent struggles for independence in the 1950s. Military disaster, loss of prestige and loss of territory by the Europeans meant that Asians began to look at them in a different and far less submissive light. The fourth period began in the mid-1960s, as the Europeans effectively disappeared off the Asia Pacific scene and the Asians themselves arrived in Europe as energetic and competitive traders and later investors. Europe was on the defensive as they were forced to look at the Asians in a new way, as effective - sometimes too effective - competitors. The balance of influence had
The fifth period began in the second half of the 1980s as the Europeans began to wake up not only to the need to get their own act together within Europe, a process which was accelerated by the collapse of communism in Eastern Europe, but also by the challenges and potentialities of the booming Asia Pacific economies. The period was one of re-exploration, particularly for the Europeans, but one in which the rising interest in regionalism in both areas and the sustained self-confidence of the Asians militated against a really balanced relationship.

But, as we approach the end of the 1990s and the start of a new century, a new period in Europe-Asia relations is about to begin. Two phenomena will act as the defining influences on this new period. The first is the development of the new format for contact at the region-to-region level, the ASEM process. The second is the setbacks to Asian Pacific regional - and, at one step removed and in a lower key, European - economic growth deriving from the financial crises which have swept the Asian Pacific region from the second half of 1997. The London ASEM summit and its follow-ups en route to ASEM 3 in Seoul in the year 2000 provide opportunities for the Europeans to show that they do care about the Asian recovery process and are willing to contribute practically and pragmatically. In the process, Asia too could come to look on Europe with new eyes and new appreciation.

Table 1 Exchange Rate Changes of Regional Currencies
(percentage change between 1 July 1997 and 1 January 1998)

<table>
<thead>
<tr>
<th>Currency</th>
<th>US dollar</th>
<th>UK pound</th>
<th>French franc</th>
<th>German Dmark</th>
</tr>
</thead>
<tbody>
<tr>
<td>Malaysian ringgit</td>
<td>-44.8</td>
<td>-34.4</td>
<td>-36.0</td>
<td>n.a.</td>
</tr>
<tr>
<td>Philippines peso</td>
<td>-41.9</td>
<td>-34.5</td>
<td>-36.5</td>
<td>-36.7</td>
</tr>
<tr>
<td>Thai baht</td>
<td>-53.7</td>
<td>-59.4</td>
<td>-49.3</td>
<td>-49.6</td>
</tr>
<tr>
<td>Indonesian rupiah</td>
<td>-69.6</td>
<td>-54.7</td>
<td>-56.0</td>
<td>-49.6</td>
</tr>
<tr>
<td>Taiwan dollar</td>
<td>-19.2</td>
<td>-12.7</td>
<td>-16.3</td>
<td>-16.9</td>
</tr>
<tr>
<td>Singapore dollar</td>
<td>-18.4</td>
<td>-14.4</td>
<td>n.a</td>
<td>-16.9</td>
</tr>
<tr>
<td>Korean won</td>
<td>-49.1</td>
<td>-44.0</td>
<td>n.a</td>
<td>-46.2</td>
</tr>
</tbody>
</table>

Sources: Asian Wall Street Journal, 8 January 1998, for rates against the US dollar; rate changes against European currencies are author's own calculations based on currency rates from Bloomberg.
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