New Zealand Asia Institute Working Paper Series

China, Southeast Asia and Economic Crises

Nicholas Tarling

NEW ZEALAND ASIA INSTITUTE
THE UNIVERSITY OF AUCKLAND
Te Whare Wānanga o Tāmaki Makaurau

No: 12-01

Abstract

'Globalisation' may be viewed as a long-term historical process. It can also be seen in two dimensions: the economic changes that have dominated the discourse of the past twenty years; but also the political changes that have made the independent nation-state a world-wide norm, very different though such states may be. The two sets of changes cannot be considered entirely separately. Some attempt to do so, however, help in an analysis of their inter-connexion. Taking both a long-term and a short-term view of the issue in general, this paper particularly focuses on China and Southeast Asia.

Author: Emeritus Professor Nicholas Tarling, LittD (Cambridge), MNZM, is a Fellow at New Zealand Asia Institute, The University of Auckland.

1 June 2012

China, Southeast Asia and Economic Crises

Nicholas Tarling

Historiography is often guided by current concerns. Viewing its outcome may thus be a guide to those concerns. That will apply to books and articles with a particular focus, such as feminism or terrorism. It will apply also to books that attempt, either with a single author or an editor marshalling other authors, to take a wider perspective, either geographically or chronologically or both. Perhaps indeed it will apply to them with particular force. The very structure of the work and the allocation of topics are problematic. Will some topics be over-emphasised, others omitted? The issue comes up even before it can be started and may not be resolved by the time it has concluded.

My own experience in producing *The Cambridge History of Southeast Asia* [1992] may without immodesty be produced as a case in point. It was to be a multi-author work, regional in focus. How were we to make the task manageable? If it were to be divided up chronologically, where would the time-lines start and stop? And on what topics should it focus, and in what order? Not all were happy with what seemed my rather conservative conclusions. Was not the Great Depression of the 1930s, they wondered, a more significant divider than the Japanese interregnum of the 1940s?

Subsequently I wrote a single-author history for OUP, *Southeast Asia: A Modern History* [2001]. It dealt with the subject regionally and topically, de-emphasising chronological divisions, but starting with the formation of states, not the economic activities of peoples. Was that putting first things first? Perhaps so: putting the state so prominently in the picture may seem more reasonable now than it did even in 2000.

In a work on regionalism in Southeast Asia that I wrote between those two dates, *Regonalism in Southeast Asia* [2006], I retained this crude and indeed ultimately unsustainable division between the political and the economic. Now I was influenced, of course, by the process and politics of 'globalisation', and I suggested that it took two forms, political and economic, both subject to ups and downs, and also interlinked in a variety of ways at various times.

The state system

The current concept of a collection of states dealing with each other on the basis of equality and in conditions of 'anarchy' - in the sense of an absence of superordinate authority - originates in Europe. It came about only after much struggle, and is often named after the treaty of 1648 that brought an end to the Thirty Years' War, Westphalia. It marked a decisive stage in the overthrow of the Holy Roman Empire and the Papacy, contenders for hegemony in medieval Europe. Instead states would conduct relations with one another on the basis of equality and sovereignty, even though their relative power differed, and their interests and ideologies often clashed.

Those struggles took place at the same time as the Europeans realised that the world was one, and they began to establish colonial realms and trading empires outside Europe. The two developments were surely connected. The urge to build and defend or expand the state in Europe was a driving force in the search for resources outside Europe. But there, of course, the Europeans did not create autonomous states on the model that was emerging in Europe. In Asia they at first treated the states they found either with deference, even awe, or on terms of equality. But in America they overthrew the empires they encountered, and established new polities whose autonomy was supported by distance rather than in principle.

That practice extended to Asia in the eighteenth and nineteenth centuries. The breakdown of the Mughal empire and the intensification of Anglo-French rivalry led to the creation of a British empire in India, though that in some ways acted as a restraint on the British elsewhere in Asia. In the nineteenth century almost all of Southeast Asia was divided among colonial powers. Japan escaped foreign intervention more narrowly, perhaps, than its historians and others have been ready to recognise. Turning 'imperialist' itself, it moved on Korea and Manchuria, in contest with the Russians who had expanded across Siberia, as well as with the Chinese. The Chinese had compromised, the Manchu achievement being either a success or a humiliation or both according to one's viewpoint. The inter-state rivalry that had promoted European expansion in the sixteenth and seventeenth centuries had been renewed by the modernisation of the state as a result of the impact of the French revolution and of industrialisation, prompting what came to be called 'imperialism'.

What had thus been created was, it might be said, a world of empires. Based in Europe, or adopting European practice, they dealt with each other on the basis of the principles of Westphalia, expanded to take account of the acquisition of empire. One crucial issue was the respective acceptance of empires. That required - as in Europe - the drawing of frontiers. It also came to require a definition of the measure of authority that imperial authorities exercised in 'possessions' and 'protectorates'. That became particularly important when the Second German Reich, established in 1871, entered the fray. Could it accept the claims the older empires put up? The Berlin Conference of 1884-5 set out guidelines, which in fact speeded up the 'partition' of Africa and spurred on the Dutch in Southeast Asia to round out 'Netherlands India'.

The world of empires could not, however, endure. Industrialisation redistributed power and that fostered ambition and apprehension. Empires came under threat or attack from other empires or would-be empires. They were also the object of threats or attacks of a political sort. Some within the metropolis considered 'empire' illegitimate, inconsistent indeed with the national principle on which their domestic states were now based. The colonial territories themselves had begun to modernise, the metropolis extending to them administrative and developmental practices adopted in the homeland, education, the ‘rule of law’, concepts of private property, the census. But, if they were to modernise more fully, they could not do so as colonial territories. Moreover, the changes imperial rulers introduced helped to produce local elites who believed that the task was properly theirs. Within the frontiers of the world of empires, they sought to create ‘nation-states’ that, on the European model, could more fully modernise their society. By this indirect route a world of states, indeed of nation-states, would replace the world of empires, though imperialism might take new forms or the word be applied to new trends.

The world wars speeded up the process, both by weakening the leading imperial power, Britain, and by advancing the US and Russia to the rank of super-powers: both of them were opposed to ‘imperialism’, though also rivals and offering rival critiques. The world wars also prompted the founding of international organisations, the League of Nations after the first war and the United Nations after the second. The UN Charter was explicitly based on the Westphalia principles, though seeking also to transcend them. The organisation, Article 2 declared, was ‘based on the principle of the sovereign equality of all its Members’: its members were to ‘refrain in their international relations from the threat or use of force against the territorial integrity or political independence of any State’. Gaining a seat in the UN was to become a significant step for a new ‘nation’: it marked a form of recognition in addition to the normal diplomatic recognition in the Westphalia tradition; and it offered a measure of security in return for the obligations it imposed.

In the Cold War world that US-Soviet Union rivalry produced, inter-state relations were intensely affected by ideology as well as interest. That affected both diplomatic recognition and seating in the UN, notably in the case of China. The seat was held by the Nationalist government for more than two decades after it had been displaced on the mainland by the Communist government. The latter took care, however, to assert that it abided by the principles that underlay the UN Charter. Indeed, in an agreement with India in 1954, it spelled them out. The preamble declared that the governing principles should be mutual respect for sovereignty and territorial integrity, non-aggression, non-interference in each other’s internal affairs, equality and mutual benefit, and peaceful co-existence. Those principles, as Coral Bell puts it, were ‘unexceptionable sentiments’.[1] Indeed they were core principles for a world of states, an amplified echo of those that underpinned the UN itself. The People’s Republic of China was demonstrating that, though not a member of the UN, it deserved to be treated as one.

Not all accepted that they were more than sentiments, since the Chinese Communist Party was known to be tendering support for communist movements in Southeast Asia and elsewhere. Indeed, it was both collaborating and increasingly competing with the Soviet Union, as in fact it had been since the 1920s. Communism was an international movement allegedly based on class rather than state or nation. In practice, however, it compromised. Indeed Lenin evoked ‘national’ support in the

[1] Coral Bell, *Survey of International Affairs 1954,* OUP, 1957, p. 244.

struggle against ‘imperialism’.[2] That struggle continued after the second world war, when the SU sought to win the support of ‘new’ nations against its rival super-power. Yet, at the same time, the course of its government-to-government relations was troubled by the undertow of party-to-party relations. The same was true of the PRC. But in neither case were the two relationships entirely at odds. Threats and promises about subversion could help to keep non-communist governments in line.

The rival super-power, the US, had no party-to-party relations to complicate or support its government-to-government relations. It was, however, determined not to be defeated in the Cold War. It was better able to offer economic aid than the SU, let alone the PRC. It also sought to fight ‘subversion’ by training and support and ‘counter-subversion’. What was in fact taking place was a war that only nominally respected frontiers and sovereignties, and that sought to displace or bend ‘neutralism’ when that was professed by sovereign states. But it was a war that in a sense was fought in a framework of understandings. It tended to consolidate the nation-state principles, even as it in practice denied them. The two super-powers were fighting a limited war, seeking allies and supporters within a system. Inherited frontiers became firmer, not weaker.

The PRC - out of the system and lacking Taiwan - was restive in the 1960s, though increasingly directing its invective against the SU and its failure to confront the US. The pattern changed with the US acceptance of the PRC regime and its admission into the UN in 1971-2. These moves were deeply disadvantageous to the SU. But it continued with the forward policy on which it had embarked, both on land and sea: it invaded Afghanistan in 1979 and it deployed its navy in the South China Sea from Cam Ranh in Vietnam. Pressed by President Reagan’s Star Wars initiative, but even more, perhaps, by economic necessity, Gorbachev sought in a speech at Vladivostok in July 1986 to open the way to the normalisation of relations with the PRC, and in a further speech at Krasnoyarsk in September 1988 he looked towards an early resolution of conflicts in Asia and called for collective efforts to reduce armaments and increase security in the Asia-Pacific.[3]

The SU’s ‘overstretch’ contributed to a mounting crisis at home, and turned Gorbachev’s reform into a revolution, even precipitating the breakup of the Union in 1991. The Cold War came to an end, though not, as some suggested, history itself. It remained to be seen how the principles of a world of states would be handled in a world where one state, the US, was overwhelmingly more powerful than any other. That was important for every state. What was of particular importance in Southeast Asia was the relationship with the ‘rising’ PRC.

---

[2] Terry Martin, *The Affirmative Action Empire*, Cornell UP, 2001, ch. 1.

[3] Vladimir Rakhmanin, ‘Soviet and Russian Policy towards Southeast Asia (1986-93)’, in David Wurfel and Bruce Burton, eds, *Southeast Asia in the New World Order*, New York: St Martin’s, 1996, p. 129. *Financial Times,* 17.9.88.

Economic globalisation

The development of a world-wide economy ran alongside, interlinked and was at times at odds with the emergence of the world of states. Its origins, like the origins of the world of states, may be dated back to the late fifteenth, sixteenth and seventeenth centuries CE. Doing that, of course, must not ignore the development of supra- or intra-regional trade links in an earlier period, across Asia landward by the 'silk route', for example, or within the 'world' as known to the Ming voyagers of the early fifteenth century CE. Nor, on the other hand, should we assume that a 'world-wide' economy of the 16-17th centuries was simply an early 'globalisation', ignoring the differences between the two, over-simplifying the process, neglecting the ups-and-downs that marked this development as well as that of the world of states. And we should, of course, not forget that the states had and have a role, promoting, manipulating, facilitating the development of their economies, in control of economic trends or at their mercy or both.

When Britain signed the Elgin treaty that helped to 'open' Japan in 1858, Marx took it as a sign that 'world trade was taking a new direction'. Succumbing to historiographical temptation, he told Engels that bourgeois society 'has experienced its sixteenth century a second time - a sixteenth century which will, I hope, sound the death knell of bourgeois society, just as the first one thrust it into existence. The particular task of bourgeois society is the establishment of the world market, at least in outline, and of production based upon the world market. As the world is round, this seems to have been completed by the colonization of California and Australia and the opening up of China and Japan.'[4]

Trade and the acquisition of colonial territories had so far been very much bound up with the rivalry among European states. War was carried on through trade and vice-versa. But the industrial revolution opened up a different prospect. The ideas Adam Smith put forward at the time when the American colonies were contesting British control could be generalised. Why, he had asked, insist on political control? Instead Britain should settle with the colonies 'such a treaty of commerce as would effectually secure to her a free trade, more advantageous to the great body of the people ... than the monopoly which she at present enjoys'.[5]

With industrialisation, the cause of free trade was widened, and imperial control seemed ever less necessary. 'Commerce is the grand panacea', Richard Cobden claimed.[6] Friedrich List was lost in admiration of Britain's achievement as the first industrial power. '[T]he world has never witnessed a

---

[4] Quoted in Dona Torr, introduction to *Marx on China,* London: Lawrence and Wishart, 1951, p. xvi.

[5] Quoted in G. Bennett, ed., *The Concept of Empire,* London: Black, 1962, p. 47.

[6] Quoted in Martin J. Wiener, *English Culture and the Decline of the Industrial Spirit,* CUP, 1981, p. 28.

supremacy to be compared with that existing in our time', he wrote in 1841. Earlier powers had sought to 'establish universal dominion upon the power of arms'. England [sic] sought to become 'an immense manufacturing and commercial city', a centre of arts and knowledge, 'the arsenal of extensive capital, the universal banker'.[7]

Arguably other nations, however, would also benefit from the 'panacea', and free trade was advanced by a range of 'most-favoured-nation' treaties. But, while industrialisation spread, it spread differentially. It began to create a new distribution of power among states, and new patterns of rivalry. It also promoted a new protectionism, not merely in respect of colonial territories, but in respect of metropolitan states. The British stood by 'free trade'. But over against them other major states resorted to protection, Germany in 1879, the US in 1890, Russia in 1891, France in 1892. The development of the world-wide economy and of the world of states crossed paths. The former did not necessarily imply free trade. That might be the choice of the leading economic power, but not of those who wished to catch up or overtake.

The first and second world wars marked further steps in the redistribution of power, breaking down the primacy of the British, but not to the advantage of their challenger on the continent, the Germans, nor their ally cum challenger in Asia, the Japanese, who, after the 'Restoration' of 1868, had adopted a programme of industrialisation and 'modernisation'. Out of these conflicts, indeed, emerged what the Germans and the Japanese had feared, two super-powers, the US and the SU. Another way of viewing the history of this period is conceivable, as the contributors to the Cambridge History pointed out. A long phase of economic expansion - marked only by occasional recessions - had been brought to a halt by the Great Depression after 1929. Was the one change more important than the other? It may be better to suggest that they interlinked in Japan and in Germany, in the US and the UK. In the depression states gained new powers and responsibilities, often sharing common problems, but framing their answers in differing ideologies.

The post-war decades

Differing ideologies were also adopted by the two super-powers at the end of the war, not only in the political field, but in the economic field also. The statesmen of the 'Western world' sought to provide international institutions that would promote economic recovery and development, and so remove the burden of depression and unemployment often seen - though it was only a partial truth - as a root cause of war. Though prepared to join the UN, the SU, on the other hand, saw it 'an institution to give security by political rather than economic means. Its own economy was so closely

[7] Quoted in B. Semmel, *Imperialism and Social Reform,* London: Allen and Unwin, 1960, p. 141.

controlled that it was unwilling either to contribute to or receive from international economic institutions.'[8]

Though it took part in regional commissions, such as ECAFE, the SU did not join in the work of other specialised agencies. Partly as a result, those connected with international trade and finance 'developed into institutions with only a loose connexion with the UN',[9] and their nature was determined by post-war discussions between the US and the UK. The interests and attitudes of those two states indeed differed, as did their resources. Abandoning the isolationism of the 1930s, and conscious of their economic strength, the Americans argued that the universal liberalisation of trade would lead to world prosperity. 'They were not opposed to the formation of customs unions, with free internal trade and a common external tariff, although these were less desirable than world-wide reduction of tariffs; but they were opposed to discriminatory tariffs.' In the Depression of the 1930s, however, the British had rather belatedly developed a system of imperial preferences. They also thought that liberalisation was not enough in itself: it had to be 'accompanied by policies designed to safeguard countries like Britain from foreign depression and slump'.[10]

The two partners recognised, however, that 'any plans to stabilize the post-war international economy must cover exchange stability and balance-of-payments problems; long-term investment; the reduction of trade barriers; measures to secure full employment; price control for primary products.'[11] The conference at Bretton Woods in July 1944 covered the first two issues. International monetary stability, it was considered, 'depended on each country having access at known rates to other currencies as part of its general liquidity position'. Each would also have to 'maintain exchange rates with a sense of responsibility towards the international economy as a whole', avoiding competitive devaluations, multiple exchange rates and anomalous cross-rates, 'while retaining an acceptable means of adjusting its exchange rate other than being forced to deflate or inflate in order to keep the exchange rate constant'.[12] The instrument was the IMF. Each member agreed a gold par value for its currency, adjustable beyond 1% only with IMF consent. The Fund, the resources of which were provided by quota contributions from each member, was also a kind of banker, though, not having its own money, it could not be a lender of last resort.[13]

---

[8] W. Knapp, *A History of War and Peace,* OUP, 1967, p. 552.

[9] ibid., p. 553.

[10] ibid., p. 554.

[11] ibid., p. 555.

[12] ibid., p. 556.

[13] Charles P. Kindleberger and Robert Z. Aliber, *Manias, Panics, and Crashes*, Basingstoke: Palgrave Macmillan, 2005, p. 229.

Bretton Woods also set up the World Bank [International Bank for Reconstruction and Development, IBRD], again sustained by quota contributions, in general the same as the contribution to the IMF, though in the US case larger. Its task was to decide what loans to give and what projects to favour. It did in the event come to focus on infrastructural projects insufficiently attractive to the private sector. Its assessment of such projects gave it another significant role, the provision of advice to 'developing' countries.

Britain and the US also agreed on proposals for an international conference on trade and employment, the two other issues, but here there were important differences. Lord Keynes, the British negotiator, 'at first denounced the American attachment to non-discrimination in trade', and then celebrated it.[14] 'Discrimination', he declared, called up 'all the old lumber, most-favored nation clause and all the rest which ... made such a hash of the old world.' The aim was to restore multilateral trade.[15]

The concerns of the British over multilateralism had, however, been increased by the negotiations for a US loan in 1945, and they did not believe that the Administration's offer of major tariff reductions would survive Congress. The Charter of an ITO was indeed signed in March 1948, but it was not ratified. The Geneva Conference that had drawn up the charter in 1947 did, however, produce a General Agreement on Tariffs and Trade [GATT], which many countries eventually signed. That forbade quantitative restrictions, except where required to safeguard the balance of payments, to protect agriculture or to assist underdeveloped countries. Tariffs were to be reduced by bargaining. The first round took place at Geneva, and others followed.

The US was a clear supporter of multilateralism in trade in the first two post-war decades. Though no ITO had been set up, a great deal was done by GATT and its secretariat, formally known as the Interim Commission for the ITO.[16] GATT evolved into a de facto world trade organisation and rounds of talks were held under its auspices following the first Geneva round, the Annecy round (1949), the Torquay round (1951), a second Geneva round (1956), the Dillon round (1960-1), the Kennedy round (1964-7), the Tokyo round (1973-90), and the Uruguay round (1986-94), which finally established the WTO.

---

[14] Jagdish Bhagwati, 'Regionalism and Multilateralism: an Overview', in Jaime de Melo and Arvind Panagariya, eds, *New Dimensions in Regional Integration,* CUP, 1993, p. 22.

[15] Quoted in ibid., pp. 22-3.

[16] Bernard M. Hoekman and Michael M. Kostecki, *The Political Economy of the World Trading System,* OUP, 1995, p. 13.

Through GATT-negotiated tariff reductions, '[e]normous progress' was made towards global free trade. Between 1947 and the close of the Tokyo round of GATT talks in 1979, the average US tariff had declined by nearly 92%, and on the eve of the Uruguay round in 1987 the average US tariff was 4.9%, the EC 6% and Japan 5.4%. They key was the most-favoured nation clause, under which bilateral bargains became available to all.[17] By 1994 tariffs had fallen further, and a range of other issues were involved, including investment, trade in 'services', and 'intellectual property'. GATT had, moreover, become quasi-universal. It now had 128 signatories, and the post-SU Russian Federation, China and Taiwan were engaged in accession negotiations.

US business, more efficient than any competitors in Europe, had seen the opportunities in a stable and open market. From the early twentieth century it had taken the lead in mass production, benefiting from a large domestic market, largely kept closed.[18] Now that lead was eroded both by the EEC and then by Japan as well, though the US had favoured their earlier growth by investment and technology transfer. Other changes in the 1970s made a range of protectionist measures more appealing, including stagflation and the rise of Asian dragons, Hong Kong, Singapore, Taiwan and South Korea. The 'new protectionism' took the form of measures that did not openly challenge GATT, but certainly challenged its spirit: border non-tariff measures [NTMs] such as voluntary export restraints [VTMs] and domestic non-tariff measures such as subsidies.

The Uruguay round concluded in Marrakesh in 1994. It was protracted not only because of the increased size of the membership but also because of the complexity of the issues it faced. Some of them were left-overs from trade liberalisation. There considerable progress was finally registered. Even more intractable, however, were the new issues, services, investment, and IPR, which the US insisted on including. The major outcome was GATS. Indeed it tended to transform the whole system by its level of intrusiveness. GATS [and TRIPS, Trade-Related IP] 'exemplify ... key parameters of deeper integration, a much more intrusive concept than traditional liberalization'. The setting up of WTO turned GATT from 'a trade agreement to a membership organisation'.[19] What conditions would a state have to meet in order to join?

The Marrakesh agreement required a WTO ministerial meeting every two years. The third, held in Seattle late 1999, was intended to review the working of the multinational trade negotiations and launch the next round. But differences among the US, the EU and Japan, and between industrialised and developing countries, bedevilled the preparatory work.[20] And outside the conference there was a new level of protest, matching in some sense the level of intrusion which the extension of GATT to

---

[17] Jaime de Melo and Arvind Panagariya, eds, *New Dimensions in Regional Integration*, CUP, 1993, p. 3.

[18] Sylvia Ostry, *The Post-Cold War Trading System*, University of Chicago Press, 1997, pp. 17, 57.

[19] ibid., p. 194.

[20] Dilip K. Das, *Global Trading System at the Crossroads,* London, New York: Routledge, 2001, p. 35.

GATS involved, but evidencing also the failure of national leaders to allow for an informed discussion of the issues and the possible outcomes. The internet globalised the logistics of mass protest and, as Rosemary Righter puts it, gave single-issue pressure groups ‘a spurious homogeneity’.[21]

Global finance

As Eric Holleiner pointed out in 1994, conventional wisdom had it that the US ‘used its overwhelming power in the early post war years to establish an open liberal international economic order’. That was not true, he argues, so far as finance was concerned: the US ‘constructed a decidedly *non*liberal financial order in which the use of capital controls was strongly endorsed’.[22] Capital controls were seen - by officials, industrialists and labour leaders, though not by private or central bankers - as ‘necessary to prevent the policy autonomy of the new interventionist welfare state from being undermined by speculative and dis-equilibrating international capital flows’.[23] It was believed - thanks to pre-war experience - that, at least in the short run, a liberal financial order would not be compatible with stable exchange rates and a liberal trading order. Also the US sympathised with financial interventionism in Western Europe and Japan for Cold War reasons.

By the early 1970s, however, the major powers had largely abandoned cooperative financing strategies, while unilateral capital controls were no longer able to handle speculative flows. ‘The ineffectiveness of capital controls reflected in part the inherent difficulties of controlling capital movements’, as Holleiner puts it. But those had now been ‘compounded by the growth of international trade and multinational corporations, which had increased the opportunities to evade controls by means of leads and tags in trade payments and in intra-firm transactions. The growth of international telecommunication links ... also made enforcement of controls more difficult.’[24] ‘The USA’, Meghnad Desai argues, ‘pursued policies during the 1960s, which a responsible key currency power should not have, but no one, and certainly not the IMF, could prevent it from doing whatever it chose to do.’[25] Though Western Europeans argued for cooperative controls, the Americans rejected them, arguing, by contrast to Bretton Woods, for the free movement of capital as well as free trade in goods and services.

---

[21] reviewing M. Moore, *A World without Walls,* CUP, 2003, in TLS, 26.9.03.

[22] Eric Holleiner, *States and the Reemergence of Global Finance,* Cornell UP, 1994, pp. 3-4.

[23] ibid., p. 4.

[24] ibid., p. 103.

[25] In M. Desai and Yahia Said, *Global Governance and Financial Crises*, London, New York: Routledge, 2004, p. 13.

Nixon's shutting the gold window was, Aglietta says, a 'purely opportunistic political move'.[26] The reason for the shift was, however, partly ideological. Argument was supplied by 'neo-liberals', drawing on Friedrich Hayek and others, who were critical of the interventionist welfare state envisaged at Bretton Woods. They also dismissed the idea that speculative capital flows would disrupt stable exchange rates by arguing for a floating exchange rate, under which speculation would not be destabilising. The other argument was supplied by 'those concerned with maintaining the [US] government's policy autonomy in the face of growing external and internal imbalances'.[27] Private investors, given the freedom to invest globally, 'would continue to underwrite U.S. deficits through their holdings of attractive U.S. assets'.[28] Other major Western countries, including the UK, accepted the neoliberal thinking, partly because of the difficulty of 'implementing national Keynesian ideas in a globally integrated financial system' and partly because of frustration over the stagflation that followed OPEC's hike in oil prices in the mid-1970s.[29] Milton Friedman seemed to have the answers.

The US renewed its enthusiasm for financial liberalism in the 1980s: 'international markets once again helped the United States to retain policy autonomy in the face of large domestic and external economic imbalances.'[30] Just as it had in the 1970s attracted investment by Arabs enriched by OPEC's oil prices, it now attracted the surplus savings of the Japanese. The UK abolished exchange controls at one blow in October 1979, and, committed to maintain London's position as an international financial centre, in October 1986 opened up the Stock Exchange to foreign securities firms [the Big Bang]. Now a substantial creditor, Japan had a stake in a stable and open global system, and also 'liberalised'. Other governments, too, began to 'liberalise' and 'deregulate', including the EC. Circumstances, example, ideology, all pointed that way.

The economic expansion of the US after 1982 and the rise in the dollar contributed to large deficits. Though financed by foreign private capital, those worried policy-makers because they contributed to protectionist sentiment. In 1985 major countries signed the Plaza accord, in which they agreed to reduce the US current account deficit by encouraging the dollar to fall. That, the Reagan Administration hoped, would improve the trade position, and encourage foreigners to bear the main burden of the deficit. Talking down the dollar would devalue the US debt, and indirectly prompt other governments to 'begin expansionary policies that would help reduce the U.S. deficit without

---

[26] Aglietta in ibid., p. 46.
[27] Holleiner, p. 120.

[28] ibid., p. 114.

[29] ibid., pp. 129-30.

[30] ibid., p. 147.

requiring the United States to reduce its growth'.[31] Initial success was followed by the collapse of the share market in October 1987.

'Globalisation' in the financial sphere, though it finally took hold, was clearly neither a smooth nor inevitable process. In it, as Holleiner shows, the state had, moreover, a major role, especially the most largest and most powerful, the US. It recognised that it 'could utilize its dominant position in the open, liberal international system to encourage foreigners both to finance and to bear the burden of adjustment to its growing current account and fiscal deficits'.[32] It was more willing to promote an open, liberal order in respect of finance than trade, because its hegemonic position lasted longer. The fact that it was also a provider of security – for example for the Arab states, as well as Japan – also supported that hegemony.

Banks and crises

With the floating of currencies, investment or merchant banks, traditionally slim operations, needed more capital, and either had to raise money on the stockmarket or join up with commercial banks. 'Commercial banks were keen to move the other way.' Their strong balance sheets gave them 'the chance to muscle investment banks out of the underwriting of securities'. The financial industry expanded. Its share of the American stockmarket climbed from 5.2% in 1980 to 23.5% in 2007.[33]

Banks' business not only grew: it became more complex. Once currencies could float, companies with costs in one and revenues in another needed to hedge exchange-rate risk, i.e take out insurance. That began a business in the early 1970s from which a complex array of derivatives emerged as the various components of risk were traded. But 'a small initial position can lead to a much larger exposure'. The biggest hiccough came after the 1987 crash, blamed in large part on a technique called portfolio insurance.

Securitisation was 'another child of the 1970s'. Loans were bundled into packages sold to outside investors. That spread the risk, gave investors more interest than government bonds, and enabled commercial banks to earn fees. They could also borrow in the markets rather than depend on the growth of retail deposits. The big market was for American mortgages. More buyers meant higher prices and slacker lending standards, including lending to low-income [high risk, 'sub-prime'] borrowers, a source of the collapse of 2008.

---

[31] ibid., p. 184.

[32] ibid., p. 202.

[33] *New Zealand Herald*, 22.10.08, p. C5, using *The Economist.*

There was 'a heavy appetite for these instruments' in Germany, Japan, and major emerging markets like China. In 2005 Ben Bernanke famously or infamously ascribed the US borrowing binge to a 'global savings glut', many emerging markets seeking to insure themselves against future crises, while oil countries sought ways to use their earnings, and countries with undeveloped financial systems, like the PRC, wanted to diversify into safe assets.[34] Bretton Woods II was the so-called Deutschebank trio's description of the system that propagated the US deficits, because the Asian countries were quasi-pegging their currencies to the dollar.[35] But you can have too much a good thing.

Greenspan, Bernanke's predecessor at the Federal Reserve Board, had spoken in December 1996 of 'irrational exuberance'.[36] The 'new economy' of dot.coms became the IT bubble that burst in 2001. But regulatory failure, insouciance, post-Cold War euphoria, a political urge to increase home ownership, talk of the end of the state, and Greenspan's own policies, prompted a crisis in the US that, like that of 1929, spread to other countries. Warnings were ignored: global current account imbalances, asset price inflation, rising household leverage, slowing output. Risks to the world economy had become extremely low, the IMF declared in April 2007.[37] Yet in 2004-06 $1.5 trillion in sub-prime mortgages had been booked.[38] The boom was fuelled by massive increases in housing prices, influx of cheap foreign capital, permissive regulatory policy, low interest rates applied after the dot-com crisis. The Bank of China was exposed to USD49 bn sub-prime Collateralized Debt Obligations.[39] Household debt in the US rose 64 times 1960-2007. US public debt stood at USD5 trillion in 2006, 44% held by foreigners. By 2009 China and Japan together held 47% of US foreign debt. China held US722bn.[40]

The bursting of this bubble had, of course, major impacts on trade, prompted higher interest rates on debt, led to bank collapses, and, less obviously, reduced government revenue from taxation. With 1929 in mind, Reinhart and Rogoff refer to a 'Second Great Contraction'. In particular it affected the export-driven economies of Asia that had benefited from America's consumer boom. The question was whether domestic demand could take up more of the slack.[41] In global crises 'exports no longer provide a cushion for growth'.[42]But how quickly can adaptation take place? The answers so far seem to have brought the state very much into the picture, even in countries where it had stood back. Are those only short-term interventions?

---

[34] Carmen M. Reinhart and Kenneth S. Rogoff, *This Time is Different*, Princeton UP, 2009, pp. 171, 209.
[35] Ibid., p. 211.
[36] Kindleberger, p. 139.
[37] Ibid., p. 214.
[38] Michael Lim Mah-Hui and Lim Chin, *Nowhere to Hide*, Singapore: ISEAS, 2010, p. 23.
[39] Ibid., p. 26.
[40] Ibid., p. 80.
[41] NZH, 31.1.09 ex Economist.
[42] Reinhart and Rogoff, p. 269.

Some argue that it should still be left to the market, as Hoover's Treasury Secretary, Andrew Mellon, had put it years before: a panic would 'purge the rottenness out of the system'.[43] But Kindleberger argues that the general rules – that state should always intervene and that it should never do so – are both wrong.[44] He talks of a lender of last resort. That, of course, applies within a country. But can there be an international one? and would it lead to - moral hazard - profligate national policies? 'If one provides insurance to everyone everywhere, with no conditions, some players are going to misbehave'.[45] Kindleberger asks in what currency it would lend: perhaps several, he answers, those with large reserve assets. When would it lend? - not when a change in currency values was in fact necessary.[46] The US as hegemon rescued Mexico in 1982. The IMF rescued Russia 1998. No one rescued Argentina in 2001. The IMF did it blunderingly in Asia 1997-8. But the G7 created no new structure except 'a talking shop', the Financial Security Forum.[47]

A world central bank would be a more efficient lender of last resort than the IMF, but 'an improbable one'. Outside the EMU most countries, including the US, see the issue of money as a mark of sovereignty.[48] Michael Aglietta points out that intrinsic LOLR problems are magnified on the international level: there is no bankruptcy court; there are no sovereign states 'to drive restructuring and to hammer out loss-sharing agreements'. 'Monetary sovereignty is over-hung by political sovereignty. And it is what is lacking in the international arena.'[49]

Or a world-wide preventative approach? Even that is at odds with world of states; and if it came about, it would surely be, like IMF, full of politics. At times strategic and financial interests coincide, for example in the case of US and the Arab world, but often they do not. States pursue interests by either means or both, and any systemic improvements have to take account of that. The most we could have may be better regulators. And could one trust in them? Consider the failure of the IMF's out of date neo-liberal approaches. And how in any case could they ensure implementation? A statement? – if that is what Kindleberger means, with investors left to draw their own conclusions.[50]

Reinhart and Roloff argue that there is 'a huge role' for international institutions in enforcing transparency. 'The task of enforcing transparency is far more easily said than done, for governments have many incentives to obfuscate their books. But if the rules are written from the outside and in advance of the next crisis, failing to follow the rules might be seen as a signal that would enforce good behavior.'[51] There is, they insist, an important role for an [new] international regulatory

[43] Quoted in Kindleberger, p. 178.
[44] Ibid., p. 13.
[45] Reinhart and Rogoff, pp. xli-xlii.
[46] Kindleberger, pp. 214-15.
[47] Desai, p. 15.
[48] Kindleberger, p. 236.
[49] In Desai, pp. 59, 64.
[50] Kindleberger, p. 254.
[51] Reinhart and Roloff, p. 282.

institution.[52] The G20 Seoul meeting was not hopeful. It demonstrated 'not collective leadership but joint abdication of power'.'[53] But perhaps more went on behind the scenes – even between the US and the PRC - than appeared in public.

Are there other longer-term possibilities? The larger non-OECD countries have potential for growth inasmuch as their work force is not so aged as that of the OECD countries, and they might attract financial savings and technology, though it would hardly be a smooth process.[54] A world currency is unlikely even long-term. But 'the world monetary oligopoly might become more complex with the rise of China, India, Indonesia, Brazil and the comeback of Russia'. They will all have 'large financial markets in national currencies, which will not be linked to any of the former key currencies'.[55] The international crisis management system would need to involve the 'South'.[56] Several 'co-anchor currencies' might emerge to dilute the hegemony of the USD.[57]

Southeast Asia

The independent states of Southeast Asia were, of course, involved in both forms of 'globalisation', economic and political. They and their leaders responded more or less creatively both to the political circumstances in which they found themselves and the economic.

Politically, their circumstances were particular as well as general. They shared the process of decolonisation with other parts of the world, but in their case it had been preceded by Japanese conquest. Their strategic value and their proximity to China subjected them to Cold War rivalries, and after its conclusion to post-Cold War uncertainties. They remained the concern of major powers and were concerned by them. Key episodes included Britain's withdrawal from its base in Singapore, announced in 1967-8; American military intervention in Vietnam, coupled with President Johnson's insistence late in 1966 that '[t]he key to Asian peace in coming generations is in Asian hands'[58] and with Nixon's Guam doctrine; the intervention and the withdrawal of the Soviet Union; the growth of China's political influence and economic power; and the various stages of the predominantly economic involvement of the Japanese.

[52] Ibid., p. 282.
[53] FT, 13.11.10.
[54] Aglietta, p. 67.
[55] Ibid., p. 67.
[56] Ibid., p. 67.
[57] Lim and Lim, p. 117.
[58] q. M. Antolik, *ASEAN and the Diplomacy of Accommodation,* Armonk: Sharpe, 1990, p. 16.

Economically, the states sought initially to break away from the colonial economic pattern by adopting ISI [import substitution] programmes, though markets were relatively small. A shift to EOI [export oriented industrialisation] gathered speed in the 1980s, backed by Japanese investment post-Plaza, and that, with in some cases the export of oil and gas, brought them extraordinary prosperity, and a growing commitment to economic liberalisation and deregulation. A vast inflow of FDI, coupled with inadequate supervision and regulation of financial markets, contributed to the economic crisis of 1997-8[59] and led - except in Malaysia's case - to the application, more or less unwillingly, of neo-liberal 'remedies'.

My fellow historians wondered whether the structure of *The Cambridge History of Southeast Asia*, which seemed to them to emphasise the role of the West, precluded an adequate account of the role of China before the Europeans arrived. That was a question no doubt partly put into their minds by the changing role of China from the late 1970s. Its 'rise' is certainly something that Southeast Asian countries take into account, both politically and economically.

How would China use the increased power that it secured through its economic expansion? The nature of the regime nurtured some apprehension. The Communist Party determined to retain its control even though it abandoned Communist ideology for the oxymoronic 'socialist market economy'. The 1989 protesters tried to appropriate patriotism.[60] Suppressing them, the regime took it over. 'Socialism' and 'patriotism' are 'by nature the same', Jiang Zemin declared.[61]

'It is not preordained that China's military power will turn into a threat, or that it will behave like the former Soviet Union', Prime Minister Goh Chok Tong of Singapore said in Beijing in 1995. But, he boldly added, 'China must show through its attitude and action that, big as it will be, it intends to be a responsible member of the international community.'[62] What Michael Leifer called its 'steely assertiveness' in the South China Sea – scene of claims and counter-claims relating both to strategic interests and oil and gas prospects – did not augur well.[63] But, as Greg Austin pointed out in 1998, there had been only two violent clashes on the ocean frontier. Beijing relied more often on 'blandishments and threats rather than use of force'.[64]

---

[59] Cf Zhang Yuejiao, 'Economic Law Reform dealing with the Asian Financial Turmoil', in Snyder, p. 286.

[60] Christopher Hughes, *Chinese Nationalism in the Global Era*, London, New York: Routledge, 2006, p. 53.

[61] Quoted in ibid., p. 58.

[62] Quoted in Storey in Lee and Storey, p. 210.

[63] M. Leifer, 'International Dynamics of One Southeast Asia', in Hadi Soesastro, ed., *One Southeast Asia in a New Regional and International Setting*, Jakarta: CSIS, 1997, p. 193.

[64] G. Austin, *China's Ocean Frontier*, St Leonards: Allen and Unwin, 1998, pp. 95, 97.

The reaction of the Southeast Asian states, moreover, prompted a ‘charm offensive’. The 1997-8 cash-and-crash crisis, too, enabled the PRC to demonstrate its goodwill. Its economic development seemed an opportunity for Southeast Asia, not a threat.[65]

China had also chosen to participate in the ARF [ASEAN Regional Forum]. The reasons were that ‘it offered it a key voice in regional politics, promoted the idea of multi-polarity and provided a way of tying other major powers such as the USA and Japan into a rule-governed community in the region’.[66] For the PRC multilateralism and multi-polarity were ‘a double-track strategy to deal with the United States’. It brought China closer to a Western way of looking at international affairs. But, as Guoguang Wu and Helen Lansdowne suggest, it was multilateralism with Chinese characteristics, designed to shape the region, expand its influence, and limit the hegemony of the US.[67]

It was responding to an opportunity ASEAN had offered, and it was a calculated offer. There was no chance that ASEAN could resist China if it chose to deploy its strength, whatever Vietnam had been able to do back in 1979: the armies of ASEAN states were national constabularies. ‘From the perspective of realist international relations theory, Southeast Asian states should have either balanced against China by forming tighter alliances with the United States, or they should have bandwagoned with China as China became more powerful. Instead, Southeast Asia did both.’[68] The US should still be involved as part of a balance of power against China. But both should be involved in a network of relationships that would cover Southeast Asia, where the ASEAN structure existed, and also Northeast Asia, where there was no such structure that could limit the potential conflicts among China, Japan, and North Korea.

‘Future historians will mark 2008 as the year that the development model that has driven much of Asia’s rapid growth for the past two decades went bankrupt’, Michael Pettis wrote in 2009.[69] Behind it lay the implicit assumption ‘that US households had an infinite capacity to borrow and spend’. That was false, and its early renewal impossible. The aim, he again suggested, should be to raise domestic consumption. China cannot do it quickly, Wen Jinbao says.[70] Can China’s neighbours do it at all, given that they have no such vast domestic markets? Perhaps a little more than may at first assumed, given their role in the value chain, i.e. making parts assembled in China. And presumably an enlarged Chinese market might also buy Southeast Asia goods, just as Americans would like it to buy US goods, raising the renminbi rate for the purpose.[71]

---

[65] Osborne, *Paramount Power*, p. 6.
[66] Alex J. Bellamy, ‘The pursuit of security in Southeast Asia’, in Mark Beeson, ed., *Contemporary Southeast Asia*, Basingstoke: Palgrave Macmillan, 2004, p. 173.
[67] Guogang Wu and Helen Lansdowne, ‘International multilateralism with Chinese characteristics’, in Wu and Lansdowne, pp. 3, 4, 7.
[68] Womack, p. 219.
[69] *Financial Times*, 20.5.09.
[70] NZH, 13.10.10.
[71] NZH, 2.6.09.

New Zealand

In remote New Zealand China bulks larger than at any previous time in its history, perhaps to the untoward neglect of Southeast Asia. But since the collapse of its special economic relationship with the UK, its commercial interests range across the world to a degree perhaps surprising in so small an economy. The Great Depression no longer remains in the personal memory of many of its inhabitants, but it remains, along with the two world wars, part of the collective memory: it played a major role, after all, in the emergence of a sense of New Zealand nationalism.

That kind of memory was certainly evoked during the 2008 depression, not merely, of course, in New Zealand. It was the worst crisis, we were told, since then; we must not go down that track again. ‘The chief practical use of history is to deliver us from plausible historical analogues’, as Lord Bryce put it. The world is now a very different place from the one into which I was born in 1931. Its states have been more active and active in different ways. Whether what memory urged them to do in haste was sufficient or appropriate we cannot yet tell. But the state is clearly not dead, and even those who thought it was, or ought to be, stopped their obsequies short, and held out their pleading hands instead.

The author acknowledges the helpful comments made by Sir Colin Maiden and Hugh Whittaker

New Zealand Asia Institute Working Paper Series

NEW ZEALAND
ASIA INSTITUTE
THE UNIVERSITY OF AUCKLAND

New Zealand Asia Institute
The University of Auckland
Private Bag 92019,
Auckland, New Zealand
Phone: 64 9 373 7999
Fax: 64 9 308 2312
www.nzai.ac.nz