

Post–Crisis Asia: Resource Mobilisation through Capital Markets, IFIs and the Private Sector

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A New Environment

We no longer have the anxiety about Asia’s future that we had 12 months ago. At the Asian Development Bank (ADB), we are optimistic about Asia’s prospects — although we are not complacent. We are optimistic because growth is on the rebound, exchange rates have stabilised, and most of the macroeconomic fundamentals are back to where they should be, with the exception perhaps of the Indonesian case. On the social front, real wages are rising and employment seems to be on the upswing, although it is still below its pre–crisis levels. However, we are not complacent, because many of Asia’s problems still remain. Three key areas of “resource mobilisation in the post–crisis era”, which is the theme of the Sixth International Forum on Asian Perspectives merit particular attention:

- domestic resource mobilisation via the capital markets;
- the role of international financial institutions (IFIs) in resource mobilisation and what might be their new role; and
- resource mobilisation through the private sector. What has happened to private flows in the post–crisis environment?

Domestic Resource Mobilisation *via* Capital Markets

The 1999 Forum focused on domestic capital markets, and one of the conclusions was that Asia was “overbanked”. To use Alan Greenspan’s phrase, the “spare tyre” of capital markets was missing. When the banking system came under stress, there was no alternative form of financial intermediation. The absence of capital markets — dubbed as “original sin” by Ricardo Hausmann — makes emerging–market

countries fragile and more exposed to economic crisis than industrial market economies: no matter how good the policy mix that they develop and use to address weaknesses, “original sin” remains and creates vulnerabilities. Hence, in Asia, the banking crisis was a fully fledged financial sector crisis, with a major impact on growth, and an increase in poverty. Another lesson from last year’s session was the need to create *demand* for capital market instruments. Liberalisation of insurance markets, pension funds, social security reform, and so on, measures that create demand for capital market instruments are key to creating this demand. A parallel observation was that governments have a major role to play in creating a *supply* of marketable instruments, and can do so by changing their borrowing and debt management policies. An important conclusion at that time was that only government could create effective benchmark instruments for the private sector. A final big message from last year’s Forum was the need to encourage transparency and disclosure in order to reinforce confidence in markets and issuers. Without transparency and disclosure, capital market development is doomed.

All these lessons remain equally relevant now, and perhaps even more so since banking markets are still fragile, but there are also new and somewhat different reasons for stressing capital market development. The “spare tyre” metaphor had to do with crisis prevention and crisis mitigation, and preventing a banking crisis from becoming a financial–sector and, ultimately, an economic crisis. With today’s increasing realisation that Asia’s population is getting older — and those of China and Japan will ultimately shrink — the “spare tyre” of capital markets is needed for other reasons as well. With more and more retirees being supported by fewer and fewer working people, increasingly, people will rely on pensions for their retirement income and no longer on the family. Those pensions will increasingly have to be funded and paid from government PAYG schemes which are often unsustainable. From this perspective, capital markets are key to success; capital–market development has a major role in supporting the demographic transition in Asia. As many Asian leaders have told us, better corporate governance and transparency in the management of assets are essential for capital markets to develop and work well: when the performance of your retirement fund depends on it, the notion of corporate governance can take on a whole new meaning.

The ADB supports corporate governance in a number of ways: in our policy dialogue with governments, and in our transactions as an investor. Governance is a criterion in screening our own private sector investments in private companies, banks, and investment funds. In sum, the “spare tyre” of capital development remains as important now as before.

Resource Mobilisation through IFIs: Post-Crisis

The IFIs still have a huge role to play in resource mobilisation for the developing countries in post-crisis Asia. However, The IFIs' role is evolving. There have been three revolutions in development banking. The first was the transition from multilateral institutions functioning as reconstruction agencies in the 1950s to their role as "project banks", focused mainly on investment loans in the 1960s and 1970s. The second revolution of the 1980s was the transition of IFIs from "project banks" to "policy banks" focusing on policy reforms — the result of a growing realisation that "policies matter" and that good projects in a bad policy environment are often not sustainable.

Now, we have the third not-yet-complete revolution, brought on by the realisation by IFIs that to be relevant to their member countries, they need to catalyse private-sector flows. Some numbers will make this clear. Twenty years ago official development assistance was of the order of \$50 billion a year, with private-sector flows to emerging markets half of that, at \$25 billion. Now, in the year 2000, private flows to emerging markets are about \$300 billion a year and official flows are down to about \$60 billion. There has not only been a reversal of the importance of official and private flows, but a complete change in the orders of magnitude of the two types of flows.

A small parable also illustrates how important the private sector has become in development finance. Imagine the head of USAID, the President of a major multilateral development bank and the Chairman of Moody's are all visiting India on the same day and the Prime Minister can see only one of them. Who would the Prime Minister see? In the 1960s, without question, it would have been the head of USAID, India's largest donor by far. In the 1980s, the Prime Minister would have seen the President of the MDB. In this century, 2000, without question, he would have chosen to see the Chairman of Moody's. The moral of this story is that the private sector is hugely important now.

In sum, the role of development banks is changing in some important ways. For example, the ADB has just prepared a new private-sector development strategy, which focuses on catalysing private flows. There are two thrusts: lending and policy advice to create a sound "enabling environment" for the domestic and foreign private sector; and, with our "private sector and transactional hat," we will play a direct role in financing selected private-sector projects.

In short, it is not just the amount of lending by development banks that matters — although it is very important that they lend and that they continue to be resourced in a significant way. More important is their role in catalysing resources and leveraging

relationships, i.e. “scaling up” partnerships, not only with the private sector but, increasingly, with other actors concerned with development — foundations, NGOs, civil society. Ideas count and development banks have a major role in creating the ideas and establishing coalitions that can help catalyse resources into developing countries. The OECD Development Centre, for example, plays an important role as a think tank for development concerns and has reached out to Latin America, ourselves in Asia, and to Africa. The IFIs will not just be lenders but, increasingly, partners with their clients, helping to share good practice and adapt ideas to local needs. Asia has done very well in absorbing best practice to create the foundation for the Asian miracle. Such ideas, together with the catalysing of resources, will be the IFIs’ new role.

Resource Mobilisation through the Private Sector

Asia was a huge success story in the area of resource mobilisation, responding to globalisation and absorbing private flows — until the crisis. There is now renewed appreciation of the private sector’s role in development as an engine of growth, and a necessary ingredient in reducing poverty. We also recognise that, while market-led growth, and the benefits of private sector development, offer a lot of promise, they are certainly not a panacea. They imply major challenges for the role of government, which needs to change in response. If government ignores the governance of companies, as has happened in some parts of the world, privatisation will not bear fruit, and neither will private sector development bring broad-based growth gains. If government ignores safety nets and society’s needs, growth will not be equitable. If government ignores corruption and lack of transparency, we will have neither growth nor equity, and, especially if government ignores the distribution of assets — not just financial assets but other assets such as education — if there is inequitable access to education, credit, and land ownership, market-led growth cannot be a good solution for the socially excluded. So, while resource mobilisation through the private sector is important, the role of government remains equally so.

On the international front, globalisation is demanding on governments. The Internet age means a whole new way of doing business for many governments. Anyone can have access to information, and at extraordinary speed. In today’s globalising world, pursuing sound macroeconomic policies is a great challenge for governments. In the social area, there is also a great demand on governments to get their expenditure priorities right — investing in their own people, investing in education, investing in health. Otherwise, the promise of globalisation will not be delivered to a broad base.

Finally, globalisation implies a huge challenge for the private sector, as well. For example, the private sector may need to involve itself in social issues — to avoid “reputational” risks, and to create legitimacy, as well as for the sustainability of its investments.

What does private sector involvement in social issues mean? A few examples may help: the ADB was recently involved in the privatisation of Manila's water supply system, where potential concessions included public stand pipes in selected slum communities where poor families had traditionally purchased trucked-in water from unreliable private parties at exorbitant prices. While clearly implying lower concession revenues for the government, this creative design resulted in close to 50 000 low-income families, over 250 000 people, having access to potable water. Furthermore, by making residents of depressed areas legitimate customers, illegal connection users were weeded out and the incidence of water theft was reduced.

Another example is an Indian company which contributed to slum upgrading in the local community, not just providing workers' housing and other benefits as is often the case, but specific investments in upgrading the city in which it was located — to create a sense of “corporate good citizenship”. In Bangkok, two major hotels have been very active in educating and training their workers to fight HIV/AIDS (including free condom distribution to staff members). The same hotels are also working with UNICEF in providing hotel and “life skills” training to young women from north-eastern Thailand, the group most likely to be forced into poverty and to engage in commercial sex work. One last example is that of a major textile company in a poor area in Pakistan, which finances schooling for its underage workers. Child employees are required to attend three to four hours of schooling in the mornings (where they also get free breakfast and lunch) before being allowed into the workplace. These are very imaginative responses to very difficult social problems, as well as very imaginative responses by the private sector. With NGOs and media looking on, not only government, but also the private sector will be playing new roles, in perhaps unexpected ways.

Post-crisis, resource mobilisation through capital markets, IFIs and the private sector will be crucial. The crisis has highlighted the importance of managing flows well, the new dimension these flows can take, and the evolving roles of IFIs, governments, and private sector over time.

