

Welcoming Remarks

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The OECD Development Centre is privileged to be organising this Forum in partnership with the Asian Development Bank for the sixth consecutive year. I am happy to be here today with my co-Chairman, Tadao Chino, President of the Asian Development Bank. I would also like to welcome Christine Wallich, Director of Infrastructure, Energy and Financial Sectors (West) of the Asian Development Bank and thank her for agreeing to say a few words to kick off the next panel, as the Dutch Minister had to cancel her trip at the last minute. Thanks to Christine, we also keep the gender balance, as we should.

The Forum is coming at a time that may be, in retrospect, a defining moment in the post-crisis period: **can we keep the momentum for reform going?**

As Ulrich Hiemenz and Tadao Chino said in their welcoming remarks one year ago, now published in the Development Centre Seminar series, much progress has been made since the onset of the crisis¹. We heard then and continue to hear now talk of rapid recovery, of rebound, of robustness. Current account balances in the region have stabilised, currencies have strengthened and investment is moderate but steady. The opening of the economies has sped up, the awareness of good corporate governance has grown and countries are increasingly focusing on their real competitive strengths.

A recent publication from the Japan Centre for International Exchange, led by Tadashi Yamamoto, on *Changing Values in Asia*², notes that the crisis of 1997–98 led Asian scholars to question whether the so-called “Asian values” were an asset or a liability. Certainly, as the same author points out in another book on *Governance and Civil Society in Japan*³, “the basic premise of the public–equals–official scheme under which the bureaucracy was seen as the exclusive arbiter of the public interest” has been shaken.

My own assessment of the Asian perspectives stresses the balance between globalisation and governance because this is indeed the guiding light of the current programme of work of the Development Centre and of the principles to be followed in 2001–2002.

Let us go back to the economic recovery, though. Regional growth forecasts have suddenly been lowered by some analysts in the financial sector. Due to the fact that the recovery is fuelled to a large extent by exports, whether the region can sustain recovery, or not, could depend on external factors such as whether the US economy continues its expansion and continues to soak up imports from Asia, or whether Japan can revive its own economy.

The US Federal reserve, by increasing interest rates, is aiming at a soft-landing for the economy slowing the rates of growth and lowering the rate of import absorption. There is light at the end of the Japanese tunnel, but whether the country will be able to return to sustained rates of economic growth in the range of 3 per cent is still a matter of speculation.

In a globalising world economy, it is hardly surprising that we see such links; that the well-being of each country depends on the expansion of the world economy as a whole.

The OECD has been highlighting these linkages for some time: our groundbreaking work at the Development Centre quantified the mutual interdependence between the OECD countries and Asia, notably the large countries: China, India and Indonesia⁴. Helmut Reisen and others examined the opportunities and challenges for sustained growth which had arisen from the emergence of the big Asian Three as “major players” on the world economic, political and environmental scene.

That study argued that today’s globalising world economy provides an historic coincidence of interests for OECD and non-OECD countries, as closer economic linkages are beneficial for sustained economic growth, for improving living standards, for eliminating poverty, and for promoting environmental sustainability.

Using a general equilibrium model, the OECD study presented two alternative scenarios of the world economy in 2020. The results showed that all countries tend to gain most from globalisation if policy reforms are pursued actively. In this way Asian countries would narrow the income gap with OECD countries. China would become the economy with the largest GDP in the world in the year 2020⁵.

The study also demonstrates that a key condition for sustained economic and social development is continued policy reform, or in other words, persistent efforts on the part of governments to improve governance. Good governance and globalisation are not simply complementary, but are necessary preconditions for each other and cannot go forward unless they do so together.

Good governance and outreach to non-OECD countries have been established as priorities for the OECD in 2001 and 2002. Governance is a complex and multifaceted issue, covering many areas. It refers to the whole economic, social and political fabric of a country. At the Development Centre considerable resources have already been directed to empirical work on governance in the public and private sector. Two examples have high relevance for Asia.

A recent study for the Centre by Shang–Jin Wei, now at The Brookings Institution in Washington, D.C., finds that corruption affects a host country's composition of capital flows in such a way that it becomes more vulnerable to a currency crisis⁶. The share of foreign direct investment is significantly reduced by corruption, while other forms of foreign finance are not. This is because international direct investors are more likely to have repeated interactions with local officials (for permits, taxes, health inspection and so on) than foreign banks or portfolio investors. This increases the need to pay bribes and to deal with extortion by local bureaucrats. Foreign direct investment also involves greater sunk costs than bank loans or portfolio flows and thus puts direct investors in a weaker bargaining position than investors in more liquid assets.

Ultimately, this is bad for growth as Reisen and Soto demonstrate⁷. Their work finds that FDI and portfolio equity investment exert a significant independent growth effect, while other forms of foreign finance can act negatively on growth in host countries with weak local financial systems.

The other relevant work is related to corporate governance. Under the auspices of the OECD/World Bank Global Corporate Governance Forum, an Asian Round Table on Corporate Governance has been initiated jointly with the Asian Development Bank. Charles Oman, who is leading our work on corporate governance and promoted a workshop where seven case studies⁸ were discussed, participated in this meeting.

It seems fair to acknowledge that each Asian country has been actively undertaking financial and corporate sector restructuring. Reform measures have been proposed or implemented in areas of corporate ownership, shareholder participation and protection, transparency and disclosure, and bankruptcy procedures, aimed at strengthening the protection of minority shareholders and creditors.

There are, however, many outstanding issues that need to be reconciled. For example, those who hold real corporate power (owner–managers) in Asia seem, in practice, if not always in word, to be less convinced of the need for significant change in local corporate–governance practices than do the many government securities–market regulators, members of the accountancy and auditing professions, heads of stock exchanges and representatives of institutes of directors and of multilateral organisations. Nor do the latter seem particularly optimistic that the sources of pressure for significant change would prevail in much of the region any time soon.

Changes have, indeed, occurred in some countries under the influence of a small number of entrepreneurs — and an equally small number of established corporate managers — who seek to attract significant extra–firm finance from international investors (especially OECD–based funds) or to sell shares in the United States (e.g. NASDAQ). For example, in India, local corporations have appreciated the fact that good corporate governance and internationally accepted standards of accounting and disclosure can help them access the US capital markets: the Indian Company Infosys made its highly successful NASDAQ issue in March 1998. Other examples abound.

The greater access to international finance markets brings benefits which go beyond the better terms offered to good projects. The scrutiny of lenders and of rating agencies improves governance and helps in sharing of experience between the firm, the sector and the whole national economy. Clearly, there are also costs: both the volume drawn from the Tenth Forum on Latin America⁹ and the proceedings of the panel on exchange rates in developing countries we organised at the Annual Bank Conference on Development Economics contain terms borrowed from other walks of life such as “sudden stop”¹⁰, “original sin”¹¹ or “fear of floating”¹². Similar analogies are visible in the recent research of Masaru Yoshitomi, a former OECD official, who helped me discover Asia some 20 years ago and whom I saw again recently as the director of the ADB Institute in Tokyo.

This is why advances in risk management are so germane to the particular combination of globalisation and governance sought by Asian countries in their strategies for recovery from the crisis. In spite of all the obstacles, technical, managerial and even political, the spread of more risk-informed judgement will help emerging markets escape from the curse of geography, something the largest continent on earth should not have trouble doing, especially if its main actors continue to combine in their own way globalisation and governance¹³.

That geography is no longer a curse is perhaps the best effect of globalisation, as long as good governance permits.

This leads us to several important questions:

- What steps can be taken to ensure that economic recovery in Asia is sustainable, even if growth should slow in the United States?
- How can we keep the momentum of reform going to improve governance?
- What are the best ways to mobilise resources, both public and private, not just for development but for equitable development?

The challenge now, taken up in the pages which follow, is to obtain a better understanding of the diverse situations in the various Asian countries and to chart the way forward.

Notes

1. Ramesh, A. and U. Hiemenz (eds.) (2000), *Achieving Financial Stability in Asia*, OECD Development Centre Seminar, OECD, Manila and Paris, pp. 9–15.
2. Han, S.–J. (ed.) (1999), *Changing Values in Asia: Their Impact on Governance and Development*, Japan Center for International Exchange, Tokyo.
3. Yamamoto, T. (ed.) (1999), *Deciding the Public Good: Governance and Civil Society in Japan*, Japan Center for International Exchange, Tokyo.
4. OECD (1997), *The World in 2020: Towards a New Global Age*, OECD, Paris and OECD Development Centre (1995), *Global Interdependence: the Links between OECD and the Main Developing Economies*, OECD, Paris.
5. Maddison, A. (1998), *Chinese Economic Performance in the Long Run*, Development Centre Study, OECD, Paris, goes in the same direction.
6. This paper draws on a study by the same author: Wei, S.–J. (1997), “How Taxing is Corruption on International Investors”, *Review of Economics and Statistics*. This paper was subsequently presented at a pre–conference on *Currency Crises Prevention*, held at the National Bureau of Economic Research in July 2000, and will be published in a conference volume edited by NBER.
7. Helmut Reisen and Marcelo Soto, in this volume.
8. See in particular the papers on corporate governance in India and China by Omkar Goswami, *The Tide Rises, Gradually: Corporate Governance in India*; and Cyril Lin, *Private Vices in Public Places: Challenges in Corporate Governance Development in China* (available upon request from charles.oman@oecd.org).
9. Hausmann, R. and U. Hiemenz (eds.), *Global Finance from a Latin American Point of View* (2000), Inter–American Development Bank and OECD, Washington and Paris.
10. See Calvo, G.A. (1998), “Capital Flows and Capital Market Crises: The Simple Economics of Sudden Stops”, *Journal of Applied Economics*, Vol. 1, No. 1, Centro de Estudios Macro–Económicos, Argentina.

See also Calvo, G.A. and C. M. Reinhart (1999), “When Capital Flows Come to a Sudden Stop: Consequences and Policy Options”, in P. Kenen, M. Mussa and A. Swoboda, *Key Issues in Reform of the International Monetary and Financial System*, IMF, Washington, D.C.

11. See Hausmann, R. (2000), "Exchange Rates Arrangements for the New Architecture", in R. Hausmann and U. Hiemenz (eds.), *Global Finance from a Latin American Viewpoint*, Development Centre Seminar, Inter-American Development Bank and OECD, Washington and Paris.
12. See Calvo, G.A. and C.M. Reinhart (2000), "Fear of Floating", paper presented at the NBER Institute; see also Calvo, G.A. (2000), "The Case for Hard Pegs in the Brave New World of Global Finance", ABCDE panel on Exchange Rates in Developing Countries.
13. José Braz in this volume explains the implications of the "risk-informed judgement".