

# Will the Crisis Divide Asia & America?

By Simon TAY

The crisis that broke from late 2008 reinforces how deeply the world is interconnected. Although the root of the financial problems was from the West, the fall in demand greatly impacts the Asian economies. Across Asia, economies that export to the United States have seen their growth taper sharply or even shrink.

Yet there are needs and opportunities for regional responses. Especially in Asia, there is potential for freer trade and closer economic integration within the region that can help offset the drastic falls elsewhere. As outlined in my previous essay (cf. pp. 42-43, May/June 2009, *Japan SPOTLIGHT*), Asian regionalism should develop in response to this crisis just as the ASEAN+3 process started in response to the earlier regional crisis of 1997.

The Chiang Mai initiative of bilateral foreign currency swaps, for example, has now developed into a \$180 billion multilateral fund to help ensure national currencies against sudden falls. Asian regionalism has momentum and growing maturity. But there is a caveat.

This crisis should not be allowed to divide Asia from America. This may not be anyone's intention. Nevertheless, division across the Pacific may emerge as an unintended consequence. Indeed, there are some signs and trends. This essay will consider this potential and unintended danger in the geopolitics that is emerging from the financial and economic crisis.

## Trends of Division

Even before the crisis, in early 2008, some were arguing that the Asian and American economies had decoupled. The crisis has shown there is no decoupling at present: when the United States has a serious problem, this affects Asia. Despite increased trade and economic integration among Asian countries, the final market for as much as 60% of Asian production remains the American market.

But the crisis may in fact end up in decoupling, with a wider and permanent gap between the two. There are three factors that point to this danger.

First, the crisis has prompted many to call on Asia to end its reliance on the American consumer and increase its own consumption. There are also calls for Asia to develop new financial mechanisms and instruments to harness its own savings for investment within the region.

This represents a considerable change from the patterns since 1997. In this period, Asian economies exported to the American market, which continued to show a strong appetite for goods. They racked up large trade surpluses and foreign exchange reserves, while the United States went into deficits at both the national and household levels. With these reserves, the Asian countries then bought and still hold US Treasury bills. This enabled the United States to enjoy a wealth effect in its assets and continue its high

levels of consumption and debt. Asians produced and saved, while Americans consumed and lived on credit.

Many now see this pattern as unnatural and unsustainable. Looking ahead, even when the United States recovers, many predict the level of US demand for Asian products will not return to what it was before the crisis. Thus, many advise that Asia must go beyond the export-led model of growth. Greater consumption in Asia is therefore seen as necessary to help the world economy and Asia itself.

But there are some who doubt that Asians can do this, especially in the short term, as they are prone to save more. With wider and stronger safety nets for their citizens, and higher wages for workers, perhaps this may be possible. But if Asians can "rebalance" their economies and become independent of the United States, there may be broader implications.

"Rebalancing" is fundamentally decoupling. The difference is only a matter of degree and attitude. If relations are affected, a sharp division across the Pacific, acrimonious divorce for two regions, may result. Should rebalancing and decoupling be Asia's goal and policy direction?

There is a second factor at play. A blame game seems to be emerging over the global crisis. Asians believe the problems lie in the United States, and the Americans point their fingers at Asia. Why?

For many in Asia, it seems clear that the problem has been speculative and ill-regulated financial derivatives that were used by the best known names on Wall Street and spread through the financial systems of the United States and Europe. There is no clear political will in the West to undertake strict and sharp reforms. In comparison, during the earlier crisis of 1997, reforms were urged and required across Asia, despite dislocation and pain. From this perspective, the United States is setting two standards for dealing with crises – one for Asians and one for itself. This double standard is hard to accept. Asians recall how, in the wake of the 1997 crisis, American standards of governance, accounting and deregulation were extolled as being the best models. This same system now seems to be at the epicenter of the crisis.

Yet instead of reform and correction, the United States seems primarily to emphasize the need for massive bailouts for companies and government stimulus packages. This is stimulus that – given the level of debt – Americans do not have reserves to pay for. Given the current patterns, described above, whereby Asians (especially Chinese and Japanese) hold their reserves in US dollars, they are the ultimate guarantors for the bailout packages. The Asians cannot control American stimulus spending, but they bankroll it. Asians from this perspective may blame the United States not only for creating this crisis, but for being inconsistent and inefficient in seeking the remedy.



*A scene from an international symposium on the Asian economy chaired by the author (center)*

Yet a growing number of voices in the United States do not emphasize faults in America. They instead emphasize the influx of funds from Asia as a driver of the crisis. In this view, the influx from Asia artificially bolstered the US economy and fed an unnatural appetite among American consumers. Combined with the extremely low cost of funds, a bubble emerged in the US market in which the financial derivatives were only the trigger that set off wider and deeper financial and economic woes. In this sense, some voices in America blame Asia for this “imbalance.” This blame game is more than an exchange of words. It feeds into a growing sense of nationalism on both sides of the Pacific. This is a third factor that can lead the crisis into dividing Asia from the United States and vice versa.

In history, sharp downturns in the economy have often been accompanied by strident and negative forms of nationalism. The urge is to blame someone else. The instinct is to unify and protect one’s own nation to the exclusion or even to the detriment of others. The present crisis is not immune to similar sentiments. A brand of nationalism is emerging in the United States. Concerns emerged from election-trail statements from then presidential candidate Barack Obama. There were also fears across Asia that the Democrats would be less in favor of trade than the Republicans had been. Such fears seem overstated.

President Obama has not become protectionist. Indeed he and his team seem very aware that protectionism triggered the Great Depression of the 1930s. Nevertheless, political nods towards protectionism have been seen. In the US stimulus package, a “buy American” proviso was inserted. Many point out the steps taken are WTO-consistent. But the move is in the wrong direction. Moreover, the United States is not to blame alone. Many in Europe and some in Asia have taken similar measures.

With the stalled Doha round at the WTO, there is little constituency for freer trade. Witness the proposed free trade agreement between the United States and South Korea. Note that the largest number of antidumping cases in the WTO is brought against imports from China, and the many complaints against goods from China because of doubts over safety and public health.

Protectionism has not come down like an iron wall across the world. But globalization and free trade have been knocked back

more than once, and from more than one source. Rather than a big bang, the ideal of freer trade may be deflated by a thousand smaller wounds and pricks.

### Why It Is Important

Isn’t it natural for Asia to depend less on the United States, have more of its own consumption, and be more “balanced”? And if Asia is decoupled and divided from the US market, should we not welcome this? Why does it matter if the crisis leads to a division between Asia and America?

Protectionism is a worry for all economies. Yet it is, as briefly described, a political reflex in this time of crisis. Even if some wish Asia to rebalance and increase its consumption, many believe it cannot be a substitute for the American market in the short term. Thus, if there is a growing division across the Pacific, dividing Asia from the United States and vice versa, the world will be bereft of one of the key engines that has driven growth in the years since the Asian crisis. There is no ready substitute for this engine.

The longer historical view also warns us of the potential price to be paid if America were to depart from Asia precipitately. The United States has been the central player in much of Asia since WWII. With the departure of the colonial powers, and the beginning of conflicts in the Cold War period, the United States emerged as the ultimate guarantor of stability and a central actor.

Economically, the United States has been the key entrant into the free markets of Asia. In many aspects, its investments and openness to trade were key drivers for the industrialization and economic transformation in the newly industrialized economies of Asia. Today, despite the rapid development in Asia, American investment and economic linkages remain very important for Asia. In security,

the US bases in South Korea and Japan are physical markers of a deeper psychological commitment to the stability and prosperity of the region.

If, therefore, the United States and Asia were to be divided in the wake of this crisis, this would be unprecedented in post-WWII history. Both would be in unrecognized territory. Some Americans may be reluctant to accept this. Others may regard this as relieving the country of burdens and costs. The American mood has been shown at times to swing towards isolationism. There are also some who see this as inevitable in the decline of the United States. Others more benignly predict a more multipolar world, even though the United States remains powerful and ahead of most others in most areas. This argument, as seen in Fareed Zakaria's "Post-American World," must still absorb the lesson that the loss of hegemony is difficult and not without consequences.

This sets the context for the United States and Asia in and emerging from the crisis: from potential isolationism and the idea of American decline to the acceptance of a more multipolar world. If isolation and decline are the dominant attitudes in the United States, the division between it and a rising and more assertive Asia will be hastened. Americans would lose out in participating in the rise of Asia that contrasts to the expected doldrums in developed world markets after the crisis.

For Asians, some may celebrate a sense of independence from American influence. More realistically, however, Asians should be concerned about the relationships amongst the rising powers in the region. Sino-Japanese relations, while currently on the mend with Prime Minister Taro Aso, have been through rocky times and fundamentally have to deal with both historical issues and the question of future leadership.

Chinese ties with India are far from settled even if the two giants have thawed in recent years. The cross-strait issue remains unresolved, as does the Korean Peninsula, and both depend greatly on the engagement of the United States.

There are, as such, considerable issues that remain for Asians to settle amongst themselves, many of which are long standing and difficult. The early and hasty retreat of American influence will not be assist in settling them. Asia is not prepared to go on its own.

### What Can Be Done

While the danger of division exists in this crisis, there are also positive signs. The change of administration is key. President Obama has emphasized a multilateral approach to the international community. State Secretary Hillary Clinton has made it a point to visit Asia on her first trip abroad. Her trip included not just the traditional allies of Japan and South Korea, but also China, which is seen as perhaps the most important US partner to address global issues. Clinton also gave attention to Southeast Asia, visiting Indonesia and also the ASEAN Secretariat in Jakarta.

Attention to Asia is the first key for the Obama administration in strengthening ties with Asia. On her visit, the secretary of state

was seen to be listening as much as speaking. And in her speeches, she was willing to bring new issues and emphases – for instance with China she explicitly decided to focus more on cooperation on climate change than on criticism over human rights.

Openness to Asian agendas is a second key. In the months following this trip, US, and indeed world, attention has returned to hot spots in Asia with, especially, the nuclear tests that North Korea conducted and Myanmar's continued persecution of Aung San Suu Kyi. The Obama administration must show the ability to address these headline issues while continuing with other engagements.

Asians can anticipate President Obama himself coming to Asia for the APEC Summit at the end of 2009 to be held in Singapore. Side trips to Japan, China and perhaps South Korea and Indonesia are also likely. Attention by Obama himself must be another effort to engage with Asia.

Beyond summitry, Asia and the United States must also define processes for their engagement. While the United States does meet with its bilateral partners and in large multilateral fora like APEC and the ARF, there is no single forum that brings the Asian and American leaderships together.

Some believe that the ASEAN-led East Asia Summit can be the venue. The summit already comprises ASEAN; China, Japan and South Korea; and also India, Australia and New Zealand. This could be expanded to include the United States permanently or as and when the occasion requires. Others have suggested new processes, like Australian Premier Kevin Rudd's notion of an Asia-Pacific community.

The search for a process and venue, however, depends on having a shared vision for Asia and the United States to go forward together. Perhaps not as they were before this crisis, but neither as "decoupled" regions that blame each other across a divided Pacific.

### Conclusion

Linked by patterns of production and consumption across the Pacific, the United States and Asia have entered this crisis together. But will they emerge from the crisis still as partners? Their demonstrated interdependence, however, is being interpreted by some as a weakness, and by others as unnatural and unhelpful, even as nationalist and protectionist sentiments rise.

Notwithstanding the history of US-Asian involvement, some now imagine a future in which Asia is more separate and divided from the United States in the wake of this crisis. Some may consider this a desirable goal for Asians. But many others may, for good reason, question such a fate. Asian regionalism can be supported. But an acrimonious and hurried division across the Pacific would be to the detriment of both.

**JS**

*Simon Tay is Chairman of the Singapore Institute of International Affairs and the 2009 Schwartz Fellow at the Asia Society in the United States.*