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# Lagarde Woos Southeast Asia as Region Cuts IMF Reliance

By Sandrine Rastello and Shamim Adam - Nov 14, 2012

Fresh from yet another meeting in Brussels on Europe's debt crisis, International Monetary Fund Managing Director Christine Lagarde today kicked off a three- country tour of Southeast Asia, which is thriving after emerging from turmoil more than a decade ago.

Her week-long visit, which starts in Malaysia and includes the Philippines and Cambodia, builds on ties that took years to mend after the 1997 Asian financial crisis forced some countries into unpopular IMF austerity policies. Now the fund is seeking to maintain its influence in a region that is helping power the world economy while reducing its reliance on the IMF's financial support.

These countries, which didn't need IMF help during the global crisis of 2008, are building up foreign currency reserves and boosting regional alliances to ensure they can weather future shocks on their own, said Eswar Prasad, a former head of the China division at the Washington-based lender.

"The main risk for the IMF is that it comes to be seen as less relevant to the region, both in terms of the advice it has to offer and in its role as provider of a financial safety net," said Prasad, now a senior fellow at the Brookings Institution in Washington.

For Lagarde, who spent most of her first 17 months at the IMF consumed by Europe's debt crisis, the trip also shows appreciation for the contribution Malaysia and the Philippines made to a $461 billion increase in the fund's resources this year, when the U.S. and Canada abstained.

## Business Leaders

The visit, which mixes meetings with officials and business leaders, concludes Nov. 20 in Cambodia with the East Asia Summit, where Lagarde will join leaders of the Association of Southeast Asian Nations and other countries, including newly re-elected U.S. President Barack Obama.

Her goal is to "engage, listen and exchange views about the global economy," Anoop Singh, who heads the IMF's Asia- Pacific department, said in a phone interview last week.

Recent economic data have shown signs of recovery in Asia. South Korea's unemployment rate fell to 3 percent in October, the lowest in more than four years, amid a rebound in the nation's exports and industrial output, a report showed today. Hong Kong may report faster year-on-year growth in the third quarter, according to a Bloomberg News survey ahead of a Nov. 16 release. The MSCI Asia Pacific Index (MXAP) rose 0.1 percent today, bringing this year's gain to about 5.5 percent.

## Confidence Rising

Australian consumer confidence surged to a 19-month high in November, a Westpac Banking Corp. and Melbourne Institute survey showed today in Sydney. The country's wage price index, which measures hourly pay rates excluding bonuses, advanced 0.7 percent in the third quarter from the previous three months, the statistics bureau said separately.

In contrast, euro-area industrial production contracted in September, a report showed today. Portugal reported a decline in gross domestic product in the third quarter. In the U.S., a report may show retail sales fell in October, a survey of economists showed. India's benchmark wholesale-price inflation unexpectedly eased to an eight-month low of 7.45 percent in October, according to a report today.

"Asia is now the global growth leader and you see how much many Asian countries have improved the fundamentals over time," Singh said. "There are clearly many lessons the world can learn from Asia."

## Lessons Learned

Some of those lessons have been learned by the IMF, which has changed its policy prescriptions since the 1990s. It has mellowed its opposition to capital controls and eased its stance on austerity measures. It now supports giving Greece and Portugal, two countries where it co-finances bailouts, more time to meet budget deficit targets.

"As we face an increasingly complex and interconnected world, we understand that the IMF needs to change and modernize, and we are doing so," Lagarde said in a speech in Kuala Lumpur today. "We are more flexible across a number of dimensions, including the time horizon for fiscal adjustment and policy responses for dealing with surges in capital flows."

The IMF arranged more than $100 billion of loans to Thailand, Indonesia and South Korea after their currencies collapsed in 1997. In return, governments were forced to cut spending, raise interest rates and sell state-owned companies. In a 1999 assessment of its performance, the fund said it "badly misgauged" the severity of the collapse and acknowledged its fiscal prescriptions for the three countries were too harsh.

"It is a very different institution than it was 15 years ago," said Joseph Stiglitz, the Nobel laureate and former World Bank chief economist who has said IMF policies in Asia during the crisis deepened the region's recession. "There is a framework for more openness," he told reporters in Singapore last week.

## 'Friendly Paradigms'

The new IMF is not lost on Anny Ratnawati, the vice finance minister of Indonesia. Then-Indonesian President Suharto was ousted in 1998 amid riots sparked by austerity measures, four months after signing an IMF agreement to scrap foreign ownership limits on banks and raise taxes on gasoline, tobacco and alcohol.

The IMF and other development partners "have come up with new friendly paradigms in managing crisis as it is now evolving in Europe and elsewhere," Ratnawati said.

"I know that the IMF has not always enjoyed a stellar reputation, particularly in this part of the world and particularly in this country," Lagarde said in Kuala Lumpur today, drawing laughter from the audience as she went on to explain how the IMF has changed.

## Investor Haven

Some of the IMF's painful policies also helped strengthen Asian economies, said Tomo Kinoshita, chief economist at Nomura Holdings Inc. in Tokyo. The region is now a haven for investors and the recipient of capital inflows after its governments spent the years since the turmoil restoring finances, bolstering banking systems and diversifying industries to increase resilience.

External debt as a percentage of gross domestic product for Asia's developing economies has dropped to 16 percent last year from about 31 percent in 1997, according to IMF data. Based on purchasing power parity, Asia excluding Japan made up about 29 percent of the world economy in 2011, compared with about 18 percent in 1997, IMF data show.

## Good Fundamentals

"Asia's fundamentals are quite good, the banking system is sound and fiscal positions are healthy, and that's partially a direct consequence of the IMF's policies," Kinoshita said.

Even now, these countries can benefit from the IMF's technical assistance and policy advice, said Prasad, also a professor at Cornell University in Ithaca, New York.

"The key issue for these economies is that they want to have the luxury of picking and choosing from the IMF's advice rather than being subjected to taking drastic measures under duress as part of the conditions associated with IMF loan programs," he said.

A precautionary credit line created by the IMF in 2009 with no conditions for countries with sound fundamentals drew no takers from Asia. The IMF will have about 80 percent of its credit in the euro region by 2014, its staff estimates.

As their economies and finances healed, Asian countries set up their own buffers against future crises, lessening dependence on the IMF and other development agencies. Asia has bolstered foreign currency reserves to more than $6.5 trillion, about 60 percent of the global total, from $485 billion in 1997.

This year, Asian policy makers doubled the size of a foreign-currency reserve pool that took effect in 2010 to shield the region from global financial shocks.

## Regional Buffers

Japan, China, South Korea and 10 Southeast Asian nations boosted the so-called Chiang Mai Initiative Multilateralization agreement to $240 billion, created a precautionary credit line to let members tap the pool to prevent a crisis, and said they would allow more funds to be used without being linked to an IMF program. The Chiang Mai Initiative has not been drawn on.

The increase reflects the region's "yes but" approach to the fund, said William Grimes, chairman of the International Relations Department at Boston University in Massachusetts. "They are more comfortable with the IMF but they're even more comfortable knowing that they might have regional options."

Lagarde's initial stop is also her first trip as IMF chief to Malaysia, which turned down the fund's assistance during the Asian currency crisis and implemented capital controls.

In some circumstances "temporary capital controls might prove useful," Lagarde said in her speech on Asian economic cooperation today. "Malaysia was ahead of the curve in this area."

## Deepening Ties

Malaysia's economy has almost tripled in size since 1997 and growth is accelerating. The government in 2010 unveiled a so-called economic transformation program, identifying $444 billion in projects from mass rail to nuclear power that it would promote in the current decade.

In her speech, which she made after meeting with Prime Minister Najib Razak and central bank governor Zeti Akhtar Aziz, Lagarde said she expects growth in Asia to accelerate next year, provided policy makers in the U.S. and in Europe make the right policy choices.

It is in Asia's interest to deepen its trade, fiscal and policy cooperation, she also said.

That cooperation is welcomed by the fund, said the IMF's Singh. "We want strong regional financial arrangements and we want to be around if our role is needed," he said. "The world is so large, the crises so complex that no region can deal with its potential crises by itself."

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