EAST ASIA KEY TO REBALANCING THE WORLD ECONOMY

By Mohamed Ariff

East Asia has been an important growth pole of the world economy for decades. There have been unmistakable signs that the centre of gravity is slowly but surely shifting from Western Europe and North America to East Asia. The so-called East Asian Miracle was predicated on an export-led growth strategy. East Asia owes its affluence to the fairly liberal market access its exports could enjoy in the rich markets of Western Europe and North America.

While there is no doubt that East Asian economies had to work hard to achieve such high growth rates, the fact remains that it was external demand that made it all possible. The United States, in particular, has played a pivotal role in all this by providing the growth thrust. The US economic growth has been fuelled by insatiable domestic demand, with Americans dangerously living beyond their means, which East Asia could take advantage of.

The upshot of all this showed up glaringly in the current account deficits of the United States and the current account surpluses of East Asian economies. This global imbalance has worked in East Asia's favour, thanks mainly to the large US capacity to endure such deficits, which was also partly due to East Asia's willingness and ability to finance these deficits.

The East Asian strategy of using its surpluses to finance the US shortfalls cannot work forever. The current global economic crisis is an inevitable outcome of the ever-widening global imbalances. The United States has been "managing" the deficit problem, but not "fixing" it. The US current account deficit of around six per cent of gross domestic product (GDP) is not a problem of the United States alone. It cannot reduce its deficits unless East Asia is also willing to reduce its surpluses. It takes two to tango.

The crux of the problem is not just that the United States is saving too little and spending too much, but East Asia, on its part, is saving too much and spending too little. To fix the problem, the US will have to save more and spend less, and East Asia will have to spend more and save less.

There in so suggestion that the United States must eliminate its current account deficit, for it only needs to reduce its deficit to a sustainable level, which is estimated to be around three per cent of GDP. This warrants painful expenditure and exchange rate adjustments on the part of the US, which is bad news for East Asian exports.

Double-digit growth rates will be clearly a thing of the past for East Asia, if it were to remain too dependent on external demand. East Asia has to rethink its growth strategy. The focus should shift from current account surpluses and foreign exchange reserves to a stable high growth trajectory. It is time East Asia learned to spawn its own internal growth impulse and dynamism.

East Asia needs to think out of the box. The track that East Asia has been treading is a dead-end. It needs to review the policy of financing US deficits, which presupposes that the US will continue to import from East Asia.

It also needs to re-examine the practice of propping up the US dollar on the premise that the strong dollar is good for not only East Asian exports but also for East Asian reserves, which are tied up in dollar-denominated assets. East Asia will be doing a great service to the global economy by importing more from the US, to close the trade gap, and by allowing the greenback to depreciate so that the US can export more.

East Asia's strategy of financing the US deficits in the interest of export growth has led to a massive movement of East Asian savings outside the region. If East Asian savings are invested within the region, East Asian economies can grow faster, driven by strong regional demand. East Asian countries can then generate demand for each other's products, which will enable them to grow faster, which in turn will fuel more demand, a recipe for increased prosperity through high growth.

This vision calls for a more liberal trade and investment regime in East Asian economies. Efforts must shift from a passive trade and investment facilitation mode to an active promotion mode.

This does not mean that East Asia must turn its back on the rest of the world. Any such move will be detrimental not only to others but also to East Asian economies themselves. East Asia should remain open to the rest of the world, importing as much from the rest of the world as they export to the rest of the world.

Put in a nutshell, East Asia can play a pivotal role in the rebalancing of the global economy by reinventing itself in such a way that will place East Asian economies firmly on the growth trajectory.

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