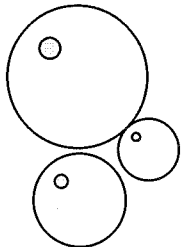
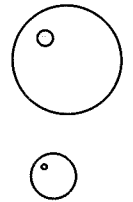
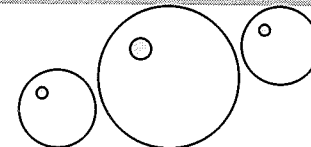


ASIA'S BUBBLE CRISIS: THE SECOND PHASE



William H Overholt
BankBoston, N.A.



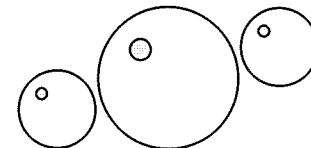
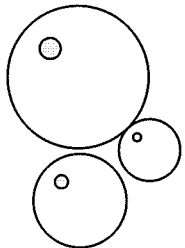
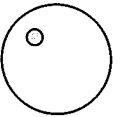
APPARENT CAUSES OF CURRENCY CRISIS

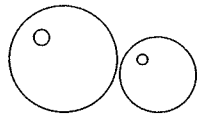
- STRONG DOLLAR
 - DUE TO JAPAN'S LOW INTEREST STRATEGY
- JAPANESE BANKS' FUNDING NEEDS
- JAPANESE ABDICATION
- CHINESE COMPETITION
- SEMICONDUCTOR PROBLEMS
- BUT THESE CHALLENGES ARE LIMITED



THE REAL ISSUE: BUBBLES & SUBSIDIZED CREDIT

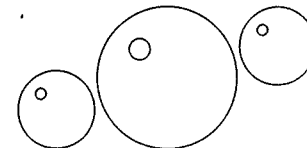
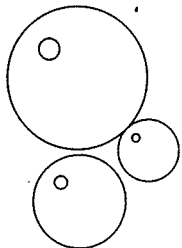
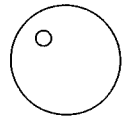
- THAILAND: REAL ESTATE
- KOREA: CHAEBOLS, LABOR
- INDONESIA: HEAVY INDUSTRY
- EVERYWHERE: BANKS
- IF INTEREST RATES RISE TO
SUPPORT CURRENCY, BUBBLES POP

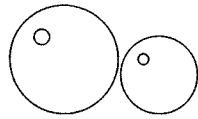




WHY DID BUBBLES PERSIST? POLITICS

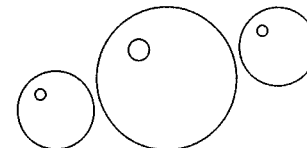
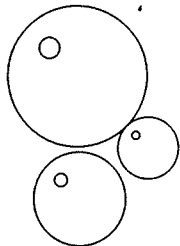
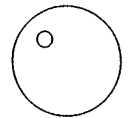
- 1 THAILAND KNEW ABOUT THE PROPERTY BUBBLE
- ⇒ KOREA KNEW ABOUT THE LABOR BUBBLE AND POLITICAL FINANCING OF CHAEBOLS
- 1 PROBLEM: LACK OF FEAR

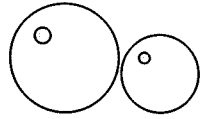




POLITICS OF THE ASIAN MIRACLE

- 1 POLITICAL MIRACLE, NOT ECONOMIC
- 1 THREATENED COUNTRIES ROSE TO THE OCCASION
 - OR COLLAPSED
- 1 NON-THREATENED HAD POLITICS AS USUAL
 - PHILIPPINES
- 1 NOW FEAR HAS LARGELY DISSIPATED
 - DEMOCRACY
 - RELAXED MANAGEMENT
- 1 SENSE OF URGENCY REMAINS IN GREATER CHINA

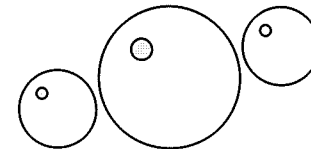
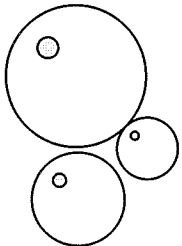
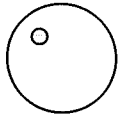


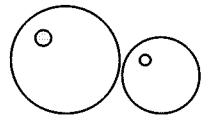


TWO MODELS OF RESOLUTION

1 US: RTC

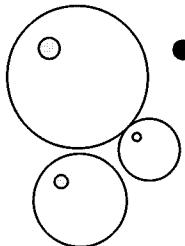
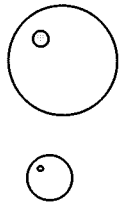
1 JAPAN: SLOW THE PAIN





REQUIREMENTS FOR BUBBLE RESOLUTION

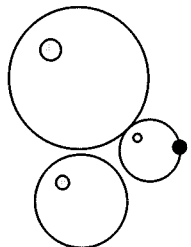
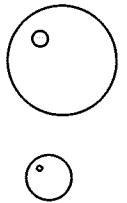
- FULL DEFLATION OF BUBBLES
 - E.G., THAI PROPERTY
- CLOSE WEAK FINANCIAL INSTITUTIONS
 - ALLOCATE LOSSES
- GET BAD ASSETS OFF BOOKS
- INJECT ADEQUATE TEMPORARY LIQUIDITY
- RESTORE COMPETITIVE DISCIPLINES

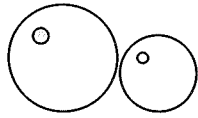




STATUS OF THE ASIAN CRISIS I

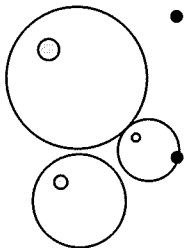
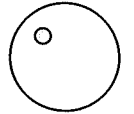
- **MOST COUNTRIES HAD FINANCIAL BUBBLES**
- **-- SECTORS WHERE CHEAP OR ALLOCATED CREDIT HAD LED TO GROSS OVERINVESTMENT OR INFLATED PRICES**
- **THE MAJOR BUBBLES HAVE BURST**
- **-- CHINA IS THE SOLE MAJOR EXCEPTION**
- **IMF PROGRAMS HAVE BEEN ACCEPTED BY ALL CRISIS COUNTRIES**
- **QUASI-IMF PROGRAMS HAVE BEEN IMPLEMENTED BY NEAR-CRISIS COUNTRIES**
- **WITH LIMITED CAVEATS, THE PROGRAMS HAVE BEEN SERIOUSLY IMPLEMENTED**





STATUS OF THE ASIAN CRISIS II

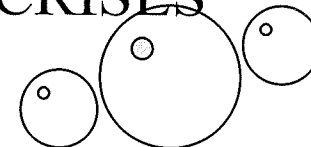
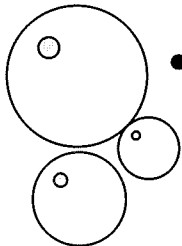
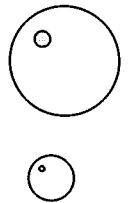
- **FINANCIAL MARKETS HAVE STABILIZED IN RELATIVE TERMS**
- **MOST DISTRESS OF THE REAL ECONOMIES, HOWEVER, LIES IN THE FUTURE -- NEGATIVE GROWTH, HIGH INFLATION, HIGH UNEMPLOYMENT**
- **THE TOUGH REFORM DECISIONS ALSO LIE IN THE FUTURE**
- **-- FOREIGN OWNERSHIP OF BANKS AND LAND, CREDITOR RIGHTS TO SEIZE PROPERTY,..**
- **HENCE THE WORST POLITICAL STRESSES LIE IN THE FUTURE**
- **IF MOMENTUM OF REFORM LAGS, THERE IS A RISK OF ANOTHER ROUND OF TROUBLE**
- **MARKETS ARE AHEAD OF THEMSELVES; HAVE RISEN AS IF REFORM SUCCESS HAS BEEN GUARANTEED; FEW BUYS IN REGION**





TIERS OF DISTRESS I

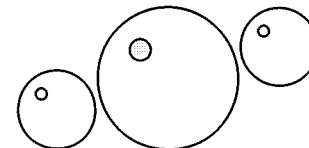
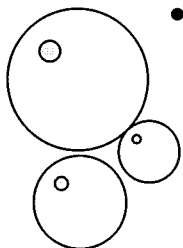
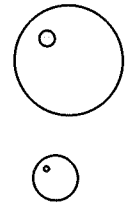
- CHINA
 - SOE BUBBLES NOT YET DEFLATED
 - PROACTIVE MANAGEMENT
 - RESULTS WILL CLARIFY IN 1999
 - CURRENCY STABLE 1998, WEAK 1999
- TAIWAN: SMALL STOCK BUBBLE DEFLATED
- HONG KONG, SINGAPORE
 - BUBBLES 75% DEFLATED
 - ADJUSTMENT QUICK
 - WEALTH EFFECTS IMPLY RECESSIONS
- MALAYSIA, PHILIPPINES
 - SMALLER BUBBLES, SMALLER CRISES
 - ESTRADA UNCERTAINTIES

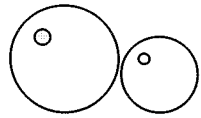




TIERS OF DISTRESS II

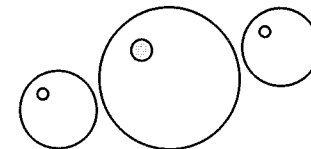
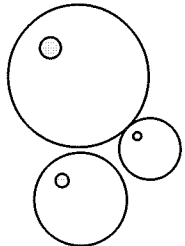
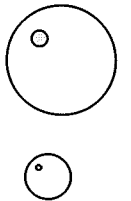
- **KOREA, THAILAND**
 - **WORST BUBBLES**
 - **STRONG INITIAL REFORM THRUST**
 - **PROPERTY, DEBT MARKETS STILL NOT CLEARING**
 - **FINANCIAL SYSTEMS LARGELY IMMOBILIZED**
 - **REAL ECONOMIES DETERIORATING RAPIDLY**
 - **3 TO 5 TOUGH YEARS AHEAD**
- **INDONESIA**
 - **LAST OCTOBER, THE PROACTIVE REFORMER**
 - **NOW, POLITICAL INFARCTION, FINANCIAL COLLAPSE**
 - **FUTURE UNPREDICTABLE**
- **JAPAN**
 - **TOO FAT TO STARVE, TOO FAT TO REFORM**

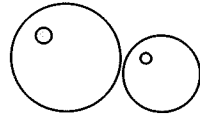




CRISIS PHASE TWO

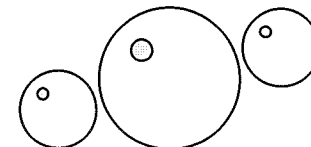
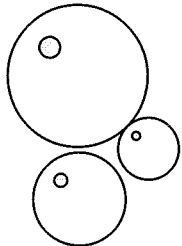
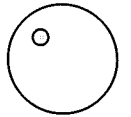
- JAPAN FAILS TO REFORM
- CHINA'S REFORMS DEFLATIONARY
- HONG KONG PROPERTY SLIDE II
- THAILAND, KOREA TRY HALF MEASURES
- INDONESIAN POLITICS PHASE II

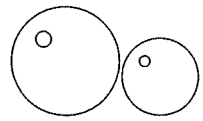




RECOVERY ASSUMPTIONS

- JAPAN DOES NOT COLLAPSE
- CHINESE REFORM ADEQUATE TO SAVE BANKING SYSTEM
- U.S. GROWTH STRONG FOR 3 YEARS
- U.S. CAN ACCEPT \$250B DEFICITS
- THAI, KOREAN REFORM PROGRAMS FOLLOW THROUGH





RESIDUAL ASIAN STRENGTHS

1 HIGH SAVINGS

1 HIGH EDUCATION

- BUT NOT THAILAND, CHINA

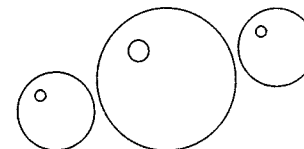
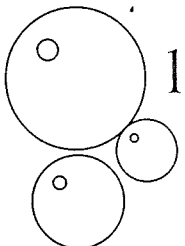
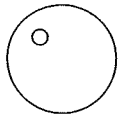
1 TECHNOCRATIC TRADITION

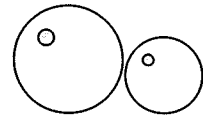
- TAIWAN CABINET FULL OF PH.D.s

1 TRADITION OF FIRM MANAGEMENT OF
PRESSURE GROUPS

- LOW INFLATION

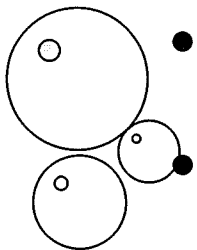
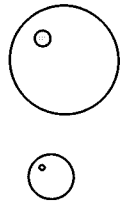
1 HENCE, WILL OUTPERFORM OVER LONG RUN,
BUT BY SMALLER MARGINS





JAPAN'S ECONOMIC ANATOMY

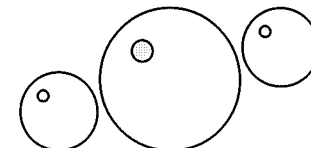
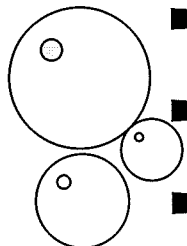
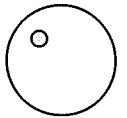
- TENNIS PLAYER'S RIGHT ARM:
CARS, CONSUMER ELECTRONICS
- GOURMAND'S BODY, RETAILING,
CONSTRUCTION, MOST OTHERS
- SMOKER'S CARCINOGENIC LUNGS:
BANKS, PROPERTY
- THE PROBLEM IS NOT CYCLICAL
FISCAL STIMULUS IS NOT A CURE





CHINA'S REFORM, 1994 - 97

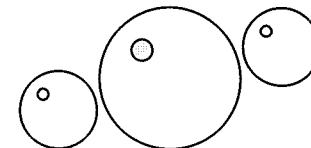
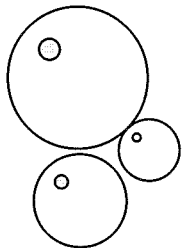
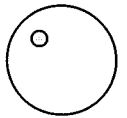
- ➔ CURRENCY REFORM
- ➔ CURRENCY STABILITY
- ➔ RESERVES \$150B
- ➔ FDI \$45B
- ➔ DISINFLATION
- ➔ HIGH GROWTH
- ➔ LEGAL REFORM
- ➔ SOE PROGRESS
- ➔ TVE SUCCESS
- ➔ BANK REFORM
- ➔ TAX REFORM
- ➔ CONSERVATIVE MOOD

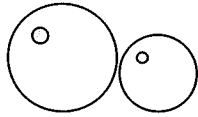




CHINA'S BUBBLES

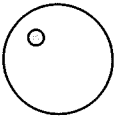
- **THE BUBBLES**
 - **BANKS: 30% NPLS, 2 TRILLION RMB**
 - **SOES: 1500 BIG BAD ONES**
- **THE HURDLE**
 - **30-40% UNEMPLOYMENT IN KEY REGIONS NOW**
 - **LABOR FORCE ADDS 13MM PER YEAR**
 - **REFORM WILL COST 30MM JOBS IN 3 YEARS**
- **THE PROGRAM**
 - **SOE DEFLATION**
 - **GOVERNMENT DEFLATION**
 - **INFRASTRUCTURE REFLATION**
 - **HOUSING REFLATION**





HONG KONG

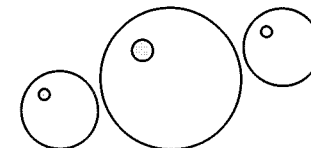
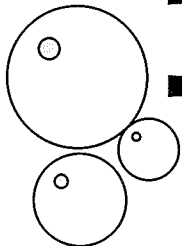
- ➔ STRONG RESERVES
- ➔ STRONG BACKING FROM CHINA
- ➔ STRONG BANKS
- ➔ STRONG PROPERTY COMPANIES
- ➔ STRONG REGULATORY SYSTEM



➔ BUT:

➔ RED CHIP BUBBLE

➔ PROPERTY BUBBLE




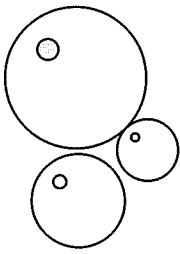



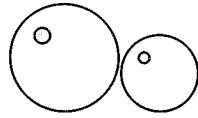
ARE THAIS, KOREANS SERIOUS?

- THAILAND

- CREDITORS ALLOWED TO FORECLOSE
 - FOREIGNERS ALLOWED TO OWN LAND
 - FOREIGNERS OWN MAJOR BANKS
- 

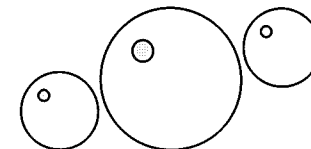
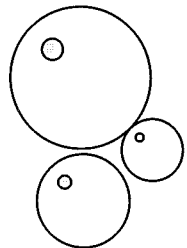
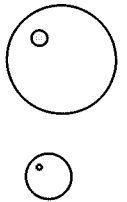
- KOREA

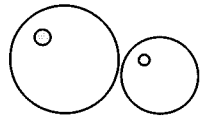
- WORKER LAYOFFS PERMITTED
 - MASSIVE UNEMPLOYMENT INSURANCE
 - BANKRUPTCY LEADS TO LIQUIDATION
 - GOVERNMENT STOPS TELLING BANKS TO ROLL LOANS TO SMEs
 - TOP 5 CHAEBOLS CONTRACT SCOPE OF BUSINESS
- 
- 
- 



CURRENCY ISSUES

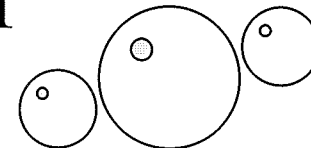
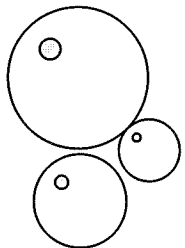
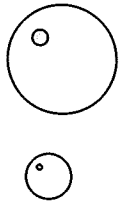
- CHINA NEED NOT DEVALUE IN 1998
- PROBABLY WILL IN 1999--SMALL
- HONG KONG NOT AFFECTED BY CHINESE DEVALUATION
- HONG CAN CAN MAINTAIN THE PEG
- WON IS BECOMING DISCONNECTED FROM YEN





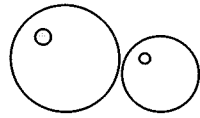
FOUR SCENARIOS

- PERFECTION OF ASIAN CAPITALISM
 - KOREAN ECONOMY LIKE BRITAIN'S
- JAPANESE-LED DEPRESSION
- JAPAN-STYLE FOOT-DRAGGING
 - KOREAN ECONOMY LIKE JAPAN'S
- CHINESE-STYLE PROACTIVFE REFORM
 - ASIA RESUMES DYNAMISM



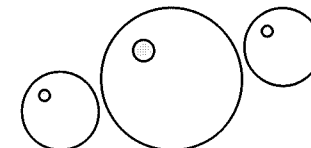
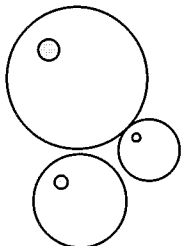
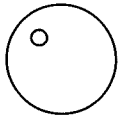
APPARENT CAUSES OF CURRENCY CRISIS

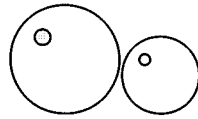
- STRONG DOLLAR
 - DUE TO JAPAN'S LOW INTEREST STRATEGY
- JAPANESE BANKS' FUNDING NEEDS
- JAPANESE ABDICATION
- CHINESE COMPETITION
- SEMICONDUCTOR PROBLEMS
- BUT THESE CHALLENGES ARE LIMITED



WHY DID BUBBLES PERSIST? POLITICS

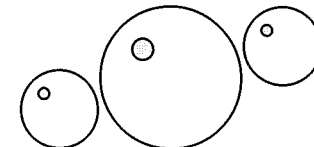
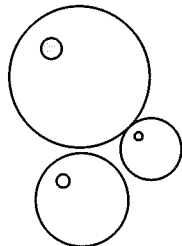
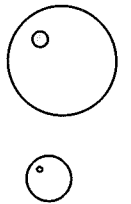
- 1 THAILAND KNEW ABOUT THE PROPERTY BUBBLE
- ⇒ KOREA KNEW ABOUT THE LABOR BUBBLE AND POLITICAL FINANCING OF CHAEBOLS
- 1 PROBLEM: LACK OF FEAR

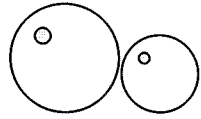




POLITICS OF THE ASIAN MIRACLE

- 1 POLITICAL MIRACLE, NOT ECONOMIC
- 1 THREATENED COUNTRIES ROSE TO THE OCCASION
 - OR COLLAPSED
- 1 NON-THREATENED HAD POLITICS AS USUAL
 - PHILIPPINES
- 1 NOW FEAR HAS LARGELY DISSIPATED
 - DEMOCRACY
 - RELAXED MANAGEMENT
- 1 SENSE OF URGENCY REMAINS IN GREATER CHINA





RESIDUAL ASIAN STRENGTHS

1 HIGH SAVINGS

1 HIGH EDUCATION

- BUT NOT THAILAND, CHINA

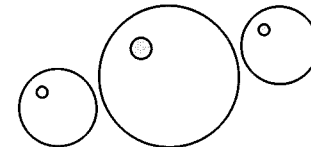
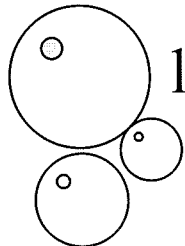
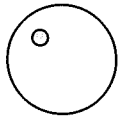
1 TECHNOCRATIC TRADITION

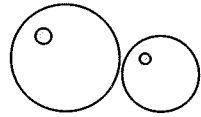
- TAIWAN CABINET FULL OF PH.D.s

1 TRADITION OF FIRM MANAGEMENT OF
PRESSURE GROUPS

- LOW INFLATION

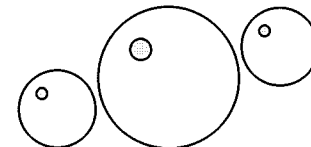
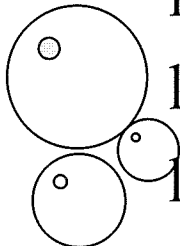
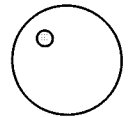
1 HENCE, WILL OUTPERFORM OVER LONG RUN,
BUT BY SMALLER MARGINS

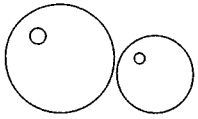




THE NEW ASIA

- 1 END OF THE AGE OF JAPAN
- 1 THE AGE OF GREATER CHINA -- MAYBE
- 1 THE GOLDEN AGE OF HONG KONG
- 1 THREE YEAR ADJUSTMENT
- 1 SOMEWHAT SLOWER GROWTH
- 1 HIGHER RISKS
- 1 HIGHER RISK PREMIA
- 1 NO LONGER AWASH WITH CHEAP MONEY
- 1 LESS OF A SELLER'S MARKET
- 1 LESS OF AN INSIDER'S MARKET





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