

Table 1.4 is also useful in verifying the fact that the depreciation of the RMB in 1994 did not harm the expansion of exports in Southeast Asia. In 1994 and 1995, all the East Asian countries had very high export growth rates. Only in 1996 did the export growth rates in all ten of the East Asian countries begin to show a decline.

4.2.3 On inflation and unemployment

Two sensitive economic indicators reflected the impact of the financial crisis. The inflation rate and the unemployment rate have risen. The former resulted from depreciation, while the latter was due to the sluggishness of the economies. Inflation rates have risen amongst two of the four dragons, Taiwan and Korea, while Hong Kong and Singapore have decreased their inflation rates. Since the Hong Kong dollar is linked to the U.S. dollar, it depreciated less, as did the Singapore dollar. The four tigers have different profiles because their currencies have been greatly depreciated, so all of them have a correspondingly high inflation rate.

Unemployment relates closely to economic recession, and as 1998 was the most serious year of the recession, with the exceptions of Taiwan and China, all the East Asian countries have seen an increase in their unemployment rates. These countries have also seen a reduction in industrial productivity and economic growth.

5. EXTERNAL DEBT AND FINANCIAL CRISIS

The relationship between external debt and economic growth is somewhat complicated. Whether external debt is good or bad for economic growth depends largely upon how we make use of it. For a developing country, usually lacking in capital, external debt plays a key role in the promotion of economic development and during the last thirty years, for example, many East Asian economies have benefited greatly from external debt. Conversely, many of the East Asian countries worst hit by the financial crisis were those

that were already saddled with heavy external debt. From the end of 1995 through until June 1997, the sum total of short-term debts in Korea accounted for 68.2%, in Thailand 66.6%, in Indonesia 60.9%, and in Malaysia 52.2%. These countries clearly have too much short-term external debt, which they must repay, together with the accrued interest, within one year. In any country where short-term debt accounted for a large proportion of total external debt, there would be greater sensitivity to changes in financial conditions. In addition, as noted earlier, many of these East Asian countries have taken advantage of short-term lending for use in long-term investments. This is simply the worst high-risk measure they could possibly take.

If the highest proportion of external debt is long-term, then this is mainly used for direct investment, which is helpful for the debtor's economic development. Correspondingly, if most of the external debt is short-term, it is mainly used for indirect investment. The importance of external debt lies not in its absolute value, but in its proportion of GDP. But even if the external debt accounts for a large proportion of GDP, this is still not a sufficient condition for the country to become drawn into financial crisis.

An example of this is Australia where, from 1990 through until 1995, external debts accounted for 46.1 percent of GDP, larger than that of Korea, Thailand or the Philippines. And yet, Australia was able to virtually ignore the penetration of the East Asian financial crisis. If, however, the short-term external debt accounts for a large proportion of total external debt, under a condition of relatively low foreign exchange reserves, this would deepen the financial crisis. This was the case in Korea, which had the largest proportion of external debt, and which also felt the worst effects of the financial crisis. (See Table 1.4).

Among the four Asian tigers, the Philippines had the largest external debt in terms of its proportion of GDP, but it suffered far less than Malaysia, Thailand and Indonesia, as well as Korea. In reality, Korea's external debt was not large in comparison to the ASEAN countries. A further example is Vietnam which has been following market economy policies for about ten years, but which was affected much less by the financial crisis.

The question arises, therefore, if a country is equipped with large foreign exchange reserves, is it in a position to avoid financial crisis? From the

Table 1.5 External Debt and Foreign Exchange Reserves

| Country | External Debt (as % of GDP) | | | Exchange Reserves (as months of imports) | | |
|-------------|--------------------------------|-------|------|---|------|------|
| | 1990-95 Avg. | 1995 | 1996 | 1990-95 Avg. | 1995 | 1996 |
| Taiwan | 0.3 | 0.2 | 0.1 | 14.5 | 11.8 | 10.3 |
| Hong Kong | | | | 9.0 | 9.1 | 10.9 |
| Singapore* | 7.7 | 8.0 | 8.2 | 6.8 | 7.0 | 7.0 |
| Korea | 10.0 | 9.4 | 11.2 | 2.8 | 3.1 | 2.8 |
| Thailand | 22.1 | 20.1 | 19.8 | 6.9 | 7.0 | 6.6 |
| Malaysia | 32.0 | 32.2 | 28.8 | 5.2 | 4.2 | 4.3 |
| Indonesia | 47.7 | 43.4 | 38.9 | 6.5 | 5.6 | 6.1 |
| Philippines | 53.6 | 50.9 | n.a. | 3.7 | 3.5 | 4.4 |
| China | 14.4 | 15.3 | 15.0 | 4.9 | 8.0 | 9.1 |
| Vietnam | 176.8 | 122.5 | n.a. | 1.4 | 2.2 | 2.1 |
| Australia | 46.1 | 46.8 | n.a. | 4.4 | 3.1 | 2.5 |

* 1993-95 average external debt estimated by Singapore Department of Statistics, Dec 1998.
Source: Ross H. McLeod and Ross Gamant (eds.) *East Asia in Crisis*, p. 26.

figures at Table 1.5, the answer is inconclusive. For instance, Thailand's exchange reserves were equivalent to 6.9 months of its imports during the period 1990-1995, and were larger than any one of the other Southeast Asian countries. Therefore, it follows that Thailand should have suffered much less from the financial crisis, however, Thailand was the one country most affected by the financial crisis!

6. CORRUPTION AND NEPOTISM BETWEEN OFFICIALS AND ENTERPRISES

In general terms, corruption may be a culture of developing countries, but corruption itself is not the main rootstock of financial crisis, although it does have the capacity to weaken the foundation of financial institutions. In East Asia, with the notable exceptions of Singapore and Hong Kong, none