

A New Financial Market Structure for East Asia

Yung Chul Park, Takatoshi Ito and Yunjong Wang (eds)

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The financial and economic crises of 1997-98 sent policy makers and economists searching for causes and lessons to prevent any recurrence of such a catastrophe. One lesson is that the region's financial systems allocate its high savings inefficiently and rely excessively on short term debt. Another is that much of the region's substantial savings are intermediated in far away financial centers rather than in the region because of market fragmentation and political and institutional barriers. This volume, a product of post-crisis conferences in 2002-03, aims to identify the means of effective and stable capital recycling within the region. Innovative and desirable though its recommendations may seem, a key issue is identified in the third chapter: the region's integration with global financial markets is far advanced; global institutions with leading edge technologies and sophisticated frameworks already have first-mover advantages in the region.

Prior to these studies, the East Asian Vision Group had recommended to the leaders of ASEAN+3 that East Asia should evolve into a common currency area '...if and when economic, political, social and other linkages develop to a point where tighter forms of monetary integration become feasible'. Not surprisingly, the studies conclude there is still much to be done to create those underlying linkages.

The conclusions are based on three sections. In the first section Barry Eichengreen, the editors, and other authors examine whether financial liberalization has increased regional financial integration using the European Union as a benchmark. The answer, based on innovative econometric analysis and examination of cross-border lending and investment by banks, is that it has but less so than in Europe where incomes are higher, intra-regional trade is higher and financial market integration has been pushed along by transnational institutions. The second section surveys regional financial centers and domestic financial markets. These chapters make it apparent that financial and capital markets are still fragmented and international financial centers in Japan, Hong Kong and Singapore are not well coordinated. Some domestic markets have developed regional specialties: Malaysia in Islamic banking and financial products, Australia in derivatives and investment banking. Korea aspires to become a regional financial hub, while other domestic financial systems are either developing (China) or require still further reform (Thailand and Indonesia).

The third part addresses the future in the context of China's continued rapid growth, Tokyo's possible decline as a regional financial center, uncertainty about Hong Kong's future set against robust performances in Singapore and Sydney. The authors recommend that governments harmonize policies, engage in mutual recognition of standards, involve the private sector, and develop a regional bond market to facilitate regional intermediation and international investment. Desirable as these measures undoubtedly are, however, the reader is left with the suspicion that such measures are not enough to

create the linkages necessary for tighter monetary integration and a regional currency and the region's integration into global markets will continue.

Wendy Dobson
Professor and Director
Institute for International Business
University of Toronto.