ECONOMIC MELTDOWN and Geopolitical Stability

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Regional Study

The Global Economic Crisis and the Development of Southeast Asia

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EXECUTIVE SUMMARY

This chapter analyzes economic growth in Southeast Asia and the impact of the current recession on countries in the region.

MAIN ARGUMENT:
Southeast Asia’s economies have been hit hard by the world recession. On the positive side, the region’s financial system, having learned from the financial crisis of 1997–98, has to a large degree avoided the types of high-risk lending and derivative investments that caused so much damage in the West. On the negative side, the global financial crisis has resulted in a serious drop in the region’s exports, thereby posing a threat to Southeast Asia’s main engine of growth.

POLICY IMPLICATIONS:
• The decline in exports and the resulting fall in the GDP growth rates for a number of countries in Southeast Asia—notably Thailand, the Philippines, Malaysia, and Indonesia—have come in the middle of a long and incomplete transition process from authoritarian to democratic forms of governance. Other countries, such as Vietnam, have retained authoritarian governance but depend on continued high growth to maintain support for the government. The impact of the global recession on exports, therefore, threatens political stability in a number of the countries in the region.
• Because the nations of Southeast Asia regularly consult with each other through the Association of Southeast Asian Nations (ASEAN), among other venues, there is little prospect of a major military action by one country in the region against another—even if the economic recession proves to be deep and prolonged.
• The U.S. can make the largest contribution to prosperity and political stability in Southeast Asia by restoring the health of the U.S. economy while remaining open to trade and investment both with the region and with the rest of the world.
Southeast Asia in late 2008 and early 2009 was, like much of the rest of the world, hit by a large man-made tsunami in the form of a worldwide financial meltdown and severe recession. The impact of this tsunami was not focused on the financial sector in Southeast Asia because the region had already experienced its own financial meltdown a decade earlier in the financial crisis of 1997–98. Many of the financial institutions in the region had been liquidated or restructured in that earlier crisis, and those remaining were cautious about taking on new high-risk financial instruments. Southeast Asia thus has not, for the most part, needed to deal with large numbers of insolvent banks, but the impact of the worldwide recession has been no less painful. The impact has instead been felt through a sharp decline in world demand for the region’s exports. The magnitude of that decline in exports has led in turn to a marked drop in the growth rates of GDP in these countries—a drop that in some cases is likely to result in negative growth rates in 2009 and possibly beyond.

This economic crisis is affecting the political situation in several of the countries of Southeast Asia, notably Indonesia, Thailand, the Philippines, Cambodia, and Malaysia, where governments and people are struggling with difficult and incomplete transitions from authoritarian to democratic governance. Other countries, notably Vietnam, have stayed with one-party authoritarian government but have needed to find alternatives to ideology and revolutionary élan to maintain political stability. The alternative that eased the
political situation for both transitioning and authoritarian governments—at least until the financial crisis of 1997–98—was rapid economic growth based on an open-economy strategy. This growth, however, was built on the foundation of weak economic institutions that made sustained high-growth rates vulnerable to a variety of external shocks. Some economic institutions were strengthened in the aftermath of the 1997–98 crisis, but most—like the political institutions in Southeast Asia—have remained weak. By making a negative impact on Southeast Asia’s exports and GDP growth rate, the current global recession is therefore likely to undermine political as well as economic stability in some of the countries in the region. The one exception among those countries pursuing an open-economy development strategy is Singapore, where both the economic and the political institutions are well-developed and strong. The odd country out in this discussion is Myanmar, which has consistently followed a closed-economy strategy, has a poor growth record partly as a result, and is governed by a brutal and highly unpopular military dictatorship that has shown no signs of losing its grip on the country, whether in good economic times or bad.

One positive note in the current situation is that Southeast Asian nations regularly consult with each other through their membership in the Association of Southeast Asian Nations (ASEAN) and related venues. There is thus little prospect of a major military action being taken by one country in the region against another even if the economic recession is deep and prolonged. Although military confrontations have occurred on the Thai-Cambodian and Thai-Myanmar borders, there is no rational reason why either situation would escalate into a major conflict. There are also insurgencies in the southern Philippines and southern Thailand, but these are localized movements within these countries. None of these conflicts come close to the Cold War divisions that existed in the region from the 1950s through the 1970s. Nor do the nations of the region have major problems with their giant neighbor to the north, China. There are marked differences concerning sovereignty over islands in the South China Sea, but there is little evidence at present that these differences could lead to a major military confrontation. India, the region’s other giant neighbor, is mainly focused on its western frontier, although New Delhi does have concerns about China’s increasing involvement in Myanmar.

The discussion of these issues that follows begins with an analysis of economic growth in Southeast Asia in the decades just prior to the recent economic meltdown. The next section then turns to an analysis of the impact of the current recession on the regional economy, followed by a section on the implications of this economic impact for the political situation. A brief analysis of the exceptional case of Myanmar will be followed by a concluding
section that outlines the interests of the United States in these economic and political trends in the region.

The Southeast Asian Economies

In the context of Asia, the various economies of Southeast Asia appear quite small. In a broader global context, however, they are not small, particularly when taken together as a region. The relevant data is presented in Table 1. In terms of GNP calculated using the exchange rate method, the Southeast Asian nations, taken as a whole, account for only 2.2% of the world total. Yet these states are trading nations for the most part, and their combined share in total world exports and imports is around 6%. This 6% figure may sound small, but it is roughly 20% greater than the international trade of Japan in 2007.1 Exports to the United States from Southeast Asia in 2005 constituted 12.5% of the region’s total exports, while exports to China and India were 8.7% and 2.5%, respectively.2 Exports to Southeast Asia in 2007 were 7.7% of China’s total exports.3 Southeast Asian trade with China in both directions, therefore, was sizeable, and the two were among each others’ major trading partners. Shares of the magnitude of the trade in both directions between Southeast Asia and China, however, do not come close to constituting a basis for a regional trading bloc or common market between the two regions as some have speculated.

A decline in income in countries such as China, Japan, and the United States has and will continue to have a measurable impact on the exports of Southeast Asia, and alternatively any resulting decline in Southeast Asian incomes will have a measurable impact on the exports of China, Japan, and the United States. Measuring the specific bilateral impact on particular countries is complex, however, and beyond the scope of this essay. At a more general and global level, a hypothetical but quite realistic 20% drop in ASEAN’s imports in 2009 would remove $150 billion or more from the demand for products from the rest of the world. Stated differently, a 20% drop in world demand for ASEAN’s exports would be equivalent to a 15% drop in ASEAN total GNP. ASEAN GNP is not likely to fall by this amount (as is discussed below), but the point is that changes in trade volume of the

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1 Japan’s exports in 2007 were $712.8 billion, or 5.1% of world exports in that year. See World Development Report 2009: Reshaping Economic Geography (Washington, D.C.: World Bank, 2009), 358–59.

2 These figures are for the year 2005 and are available from the ASEAN (Association of Southeast Asian Nations) website, “External Trade Statistics,” http://www.aseansec.org/18137.htm. These figures are the most recent compilation available on the internet from the ASEAN secretariat.

3 This figure is for 2007 and was derived from the National Statistical Office, China Statistical Yearbook 2009 (Beijing: China Statistics Press, 2009), 717.