

## **Mr Hayami: Globalization and regional cooperation in Asia**

Speech given by Mr Masaru Hayami, Governor of the Bank of Japan, at the Asian Pacific Bankers Club, in Tokyo, on 17 March 2000.

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It is a great honor to be invited today and given an opportunity to address distinguished members of the Asian Pacific Bankers Club. In particular, I would like to commend the Club for providing a valuable forum for fostering mutual understanding among representatives of major banks in East Asia and the Pacific region. More than two years have passed since the outset of the currency crisis in Asia, and we can now say that we have clearly witnessed a recovery. Thus, at this juncture, I believe it useful to examine what kind of regional cooperation is desirable in Asia from a long-term perspective.

### **Positive and negative sides of globalization**

Let me first consider globalization. The essence of globalization is the integration of markets worldwide and the deepening of various interdependent relations. As we all know, the speed of globalization has been accelerating, especially in financial markets. This is clearly evidenced by the significant increase in foreign exchange transactions and international bond issues over the span of the past ten years. You will all agree that the rapid progress of information and communication technology has played a decisive role as the driving force behind globalization.

But, we should not forget the dynamic mechanism whereby globalization creates pressures for the harmonization of such systems as accounting, taxation and corporate governance across borders, which, in turn, leads to further globalization. As is commonly said, “globalization begets globalization”. Thus, the move toward globalization is an inevitable reality, and not likely to be reversed.

Bearing in mind such a reality, we need to examine the problems related to globalization and how we should respond to them. Globalization has brought about a variety of changes. One obvious benefit from a long-term viewpoint is that active cross-border capital flows will realize the efficient allocation of world resources.

At the same time, precisely because of enhanced efficiency, there is a greater risk that the rapid increase in international capital flows will induce an unexpected adverse impact, as was the case when financial crisis contagion following the outbreak of the Asian financial crisis in 1997 spread to Russia and Latin America.

Given the fact of life that globalization is not reversible, what we need to do is to minimize the negative side of globalization. In fact, since the financial crisis in Asia, various measures have been effected to prevent international contagion stemming from financial crises and to improve the international financial system. These measures include the improvement of disclosure to achieve enhanced market discipline, the establishment of a domestic financial system which is robust and resilient to external shocks, closer international cooperation in terms of financial supervision, and the review and strengthening of IMF functions.

### **Progress of regional cooperation**

Amid globalization, it is worth noting that we have also witnessed a clear trend toward regionalism or regional cooperation in various parts of the world. These movements toward promoting regional cooperation have taken due account of trade and financial relations. For example, in Europe, the introduction of the euro and the expansion of the EU. In the Americas, the expansion of NAFTA and

dollarization which is being considered by some Latin American countries. In Asia, we have begun to observe some moves toward closer cooperation as I will describe later.

Can we reconcile these two contrasting trends, the progress of economic and financial globalization on the one hand, and the strengthening of regional cooperation on the other? One possible interpretation of this difficult question is that the driving force behind globalization has also made the interaction of economic and financial activities closer in regions which have a lot in common. For example, the rapid progress of information and communication technology can be regarded as one of the major factors supporting the integration of financial markets in the euro zone.

Therefore, globalization and regional cooperation can proceed simultaneously. Furthermore, regional cooperation, if managed properly, will promote globalization. For example, if there are problems for which it will take a long time to form a global consensus, it may be possible to reach a consensus relatively quickly among specific regions. This is a case where regional cooperation lowers barriers to globalization in countries within the regions concerned.

Furthermore, if there is a common platform for discussion or a framework for solving problems in a region which consists of countries with similar economic conditions and policy orientation, we may be able to reduce the cost of global negotiations in the event of international policy conflicts or shocks. In such a case, regional cooperation may supplement a global cooperative framework. It may sound a little ironic, but regional cooperation has become all the more significant and important when globalization progresses rapidly. The global economy of the twenty-first century will most likely be a multi-layered global network of various forms of regional cooperation.

### **Regional cooperation in Asia**

Now, I would turn to regional cooperation in Asia. Needless to say, Asia is extremely diverse in terms of culture, politics, and religion. Such diversity entails difficulties in promoting regional cooperation. In fact, the speed of regional cooperation in Asia has been slow compared to other regions. However, it is also true that the extent of interdependence has become more widespread and deep as witnessed by the progress of the horizontal division of labor and increased capital flows in East Asia. In addition, since the bitter experience of the currency crisis in 1997 has made us recognize the risk of spillover and contagion, I believe that momentum for actively promoting regional cooperation as a device to support globalization has steadily increased.

In promoting regional cooperation, let me offer you three important points in the economic and financial area. First is the strengthening of mutual surveillance. It is a major premise for any regional cooperation that the countries concerned share a common recognition with respect to the economic and financial conditions of individual countries in the region, their interdependence, and the risks inherent in the regional economy.

Second, countries in the region should share a common view of the future direction of the regional economy and also concrete policy response based on such recognition. Bearing in mind the lessons we learned from the currency crises, we should improve the functioning of financial markets and foreign exchange regimes, and also strengthen domestic financial systems and financial supervisory frameworks. In order to make an appropriate policy response, not only coordination among countries in the region but also competition among them are very much needed.

Third is participation in global efforts toward the stability of the international financial system, which is often termed the "New International Financial Architecture" problem. It seems to me increasingly important to send a coherent message from Asia to such international fora as the Financial Stability Forum, the Group of Twenty Finance Ministers and Central Bank Governors, and the International Monetary and Financial Committee.

Having said all this, we should never forget the importance of maintaining the basic philosophy of "open regionalism" as a major underlying premise to contribute to the stability and development of the world economy. Central banks also play a very important role in promoting regional cooperation. As symbolized by the rapid expansion of derivative transactions, we now live in a world where

international capital flows have become extremely complex and the speed at which a shock is transmitted across borders has accelerated.

In such a world, it is not possible for the central bank of any one country to ensure integrity of the international financial system. This can be easily understood if we recall such problems as the liquidity risk involved in foreign exchange and the Herstatt risk in cross-border settlements. To discharge the responsibility of conducting appropriate monetary policy and maintaining financial system stability as well as to prevent international systemic risk from emerging, mutual cooperation and coordination have become increasingly essential among central banks in the region.

In this context, a forum called EMEAP, composed of central banks in the East Asia and Pacific region, was established in 1991. In this forum, member central banks have been exchanging views and information regarding economic, financial market, and foreign exchange market developments. They have also been studying ways to make improvements in such areas as financial markets, settlement systems, and bank supervisory methods.

### **Conclusion**

In closing, let me briefly touch upon Japan's role in Asia. Given the size of its economic presence and close relations with countries in the Asian region, Japan should make an appropriate contribution to regional development. To this end, first of all, Japan itself must aggressively implement structural reform to realize robust economic fundamentals.

At the same time, Japan should promote further opening and improvement of its domestic markets to contribute to the efficient and fair allocation of world resources. Particularly in financial markets, various measures for improvement have been effected. For example, in the benchmark government bond market, the maturity of bonds has been diversified and the withholding tax on non-residents lifted.

We should continue such efforts to make domestic markets more attractive for overseas investors. Through such efforts, I believe and sincerely hope that countries both within and outside the Asian region will come to have greater confidence in Japan, which, in turn, will contribute to closer and stronger cooperation in Asia.