The last time a financial contagion swept through the region, it started here, in Southeast Asia. The 1997 Asian financial crisis began when the Thai government, unable to defend its currency against aggressive speculative selling, was forced to devalue the baht against the U.S. dollar. The baht collapsed and with it, the nation’s banking system, and the crisis quickly spread to South Korea, Indonesia and other parts of Asia. The culprits, as analyzed by a stern International Monetary Fund and the rest of the finger-wagging West, were poor risk management, over-leveraged and badly run financial institutions and companies, and poor corporate governance, which produced large quantities of bad assets. Many in Asia have not forgotten the image of IMF chief Michael Camdessus standing over former President Suharto of Indonesia when signing a “bailout agreement” for Indonesia.

The immediate consequences were ugly. Foreign investors rushed to withdraw their capital from the region, local currencies and stock markets collapsed and credit evaporated. The Association of Southeast Asian Nations economies suffered for years as they slowly rebuilt their financial systems and economies. While Singapore did not suffer from many of the ills that caused the crisis in other countries, it was still hurt, largely due to its physical proximity to some of the hardest hit countries, and by the general loss of confidence in the region. Many large regional companies went bankrupt or were significantly restructured. Contrite, Thailand and Indonesia looked humbly to the West for wisdom in economic policy-making.
Now, of course, the teachers have not practiced what they
preached and taken greater missteps than the students. While commentary has been muted, the irony has not
gone unnoticed. Writing in his personal blog, former
Malaysian Prime Minister Mahathir Mohamad noted: “I
remember well how we were told never to bail out failing
companies.” While political leaders are perhaps not saying
this publicly, there is a general sense in the region that
U.S. credibility and leadership has been damaged, and the
U.S. “model” needs to be re-examined. Even Singapore,
which has always viewed the U.S. as its most important
ally, will place greater importance on diversification of
relationships. Singapore’s efforts to strengthen ties with
China and India will likely be reinforced.

Southeast Asia has in fact been hit hard by the crisis; few markets or asset classes anywhere in the world have escaped unscathed. But the big difference with the West, and with 1997, is that there does not appear to be much systemic risk to regional financial institutions. Asia does not seem to be experiencing so much a financial crisis as an economic one. Asian financial institutions have not revealed any significant exposure to subprime or other toxic assets. Thus far, there have been no major bank failures, government recapitalizations, forced buyouts, or crisis-driven bank mergers. The move by Singapore, Hong Kong, Malaysia, Vietnam, Thailand and Indonesia to guarantee bank deposits was to pre-empt the possibility of rumor-sparked bank runs, and not a sign of fundamental weakness in their banks.

The losses experienced by Singapore’s sovereign wealth fund Temasek Holdings Pty. Ltd. on its investments in Merrill Lynch & Co., Barclays plc and other financial institutions in the West are a significant but manageable hit to its estimated total asset base of more than $134 billion. Yes, there has been some depreciation of regional currencies against the dollar, but they have generally held up reasonably well against other world currencies. Overall, banks across the region remain well capitalized. To date there has been only one small bank run, that on Bank of East Asia Ltd., which was easily contained.

This time around, most of the damage appears to have been sustained by companies that rely on exports to the West, by the producers of commodities or unfinished goods supplied to the exporters, and by regional financial institutions suffering collateral damage from the West. Export revenues, particularly for manufactured and electronic goods, and commodity prices are way down. Unemployment has rapidly increased. Singapore is in recession, and Malaysia, Indonesia, Thailand, and Vietnam have seen dramatic slowdowns.

The greater impact on Singapore this time is perhaps a function of how much more integrated Singapore is into the international, financial and trade system compared with the other countries of Southeast Asia. In response to the crisis, economic stimulus packages have been rolled out across the region. The packages range from more than $6 billion in both the Philippines and Vietnam to more than $3 billion in Thailand and $2 billion in both Malaysia and Indonesia.

Singapore has just announced a massive $13.7 billion plan to help save jobs and help viable companies stay afloat for this year. The budget will result in a $5.8 billion deficit, the country’s largest ever.

Political uncertainties in some Southeast Asian nations have not helped the situation. Thailand has been gripped by political turmoil since the removal of Thaksin Shinawatra by an army coup in 2006. In November antigovernment agitators closed Bangkok’s international airport for eight days. Indonesia, with 24 political parties and 150 million eligible voters, is scheduled to hold parliamentary elections in April, and a presidential election follows in July. In the Philippines, presidential elections, legislative elections and local elections are scheduled for May 2010. Current President Gloria Macapagal-Arroyo is barred from seeking re-election due to term
limits. In Malaysia, political uncertainty has surrounded Prime Minister Abdullah Ahmad Badawi’s proposed stepping down in March, and various scandals affecting high-ranking government officials also cloud the political environment.

But there is still a sense, succinctly stated in a recent HSBC plc report, that “Asia’s problems are cyclical, while the West’s problems are structural.” Some here believe that Asia will therefore rebound more quickly than the West. Is this really true, or is it just that the impact of the crisis here lags behind that in the West, so that Asia will suffer its own structural impairments? Time will tell.

One theory that seems to have been disproved by this crisis is that a “decoupling” of the Asian economies from that of the West is occurring. Clearly Asia is so inextricably connected to the West that there was no escaping the impact of the crisis. But it will be interesting to see how Asia performs when the world economy rebounds.

The World Bank estimates that most of the emerging-markets countries, including those of Southeast Asia, will still show positive growth in 2009, whereas the U.S. and Europe are projected to be in recession for quite a few quarters.

And it is noteworthy that intra-Asia trade has been growing much faster than trade with the West. ASEAN trade statistics for 2007, the most recent available, show annual trade volumes between China and ASEAN nations now to be in excess of $200 billion, where the latest corresponding statistics put trade volumes between the U.S. and ASEAN nations at $170 billion. And China, the great economic engine in the region, continues to grow, albeit at a reduced pace.

Meanwhile, Southeast Asia will need to work through the challenges of the crisis along with the rest of the world. Regional bankruptcies are mounting. The tide of restructurings will undoubtedly surge in the next few quarters as the real economy in the West founders, and this echoes through Asia. The region’s financial institutions will need to provide the capital that retreating Western banks are currently unable to supply.

As Singapore Prime Minister Lee Hsien Loong said in his New Year message: “A world in recession is not a world without opportunities. In the midst of the storm, we must keep pursuing new growth changes, and look beyond the immediate problems to ensure that Singapore emerges stronger after the downturn.” But, for the moment, there is not the sense of dire urgency, of near apocalypse, which seems to prevail in the West.

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