THE PERILOUS MOMENT

Indonesia, Australia and the Asian Crisis

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As a piece of writing and as a history, Paul Keating's 'Perilous Moment' speech describing the Asian economic crisis of 1997–98 is compelling reading for anyone interested in this crucial time in Asia and for the world economy. The speech weaves the threads of the varied and complex issues into a tapestry, which provides the reader with accessible images. It traces the history of the crisis from the first attack on the Thai baht in May 1997 to the contagion which followed, especially in Indonesia. It tells how the International Monetary Fund overplayed its hand with a complete reordering of the Indonesian economy through its intrusive program of so-called 'structural conditionality'. Paul Keating explains how this crisis affects Australia and how Australia should stand by Indonesia. Prophetically, he said with financial contagion facilitated by rapid communications, 'we are likely to have less warning of future crises—and when they come, the swings they generate are likely to be larger'.

It is ten months since we saw the first signs of the Asian economic crisis with an attack by speculators on the Thai baht in May 1997. Since then, the crisis has unravelled in unpredictable ways across Asia. It is not over yet, and it presents Australia and the other countries of the region with a complex and dangerous challenge.

That challenge is not just economic, although the implications for individual economies, including Australia's, are serious. It is political and strategic as well. The whole direction in which the Asia Pacific has been moving—towards economic and political openness, towards a sense of Pacific community—is at risk. It is a perilous moment and there are real questions in my mind about whether we and our institutions can meet it successfully.

I want to talk tonight about why the Asian economies suddenly look so shaky, why the problems seem worse in Indonesia—the country of greatest immediate concern to Australia—what the implications are for our global and regional institutions, and what Australia should be doing about it.

This is the first region-wide crisis we have seen in Asia since it became one of the central pillars of the global economic system.

No-one predicted its timing or its precise cadence. And no-one understands with certainty whether it will spread further or how long its resolution will take.

But one of the important causes certainly lies in currency exchange rates, and the impact of rapid movements of currency which the information revolution has facilitated.

Its beginnings can be traced back to 1985. That was the year when, in response to growing US concern about the size of its trade deficit with Japan, the G5 industrial countries agreed in the Plaza Accord to take coordinated policy actions to push the US dollar lower. The result of their efforts, as they intended, was that the yen appreciated strongly against the US dollar.

That rising yen increased costs for Japanese exporters and encouraged them to move off-shore. Asia was the preferred destination, in part because the pegs Asian governments had established between their currencies and the US dollar made production costs cheap.

Over the next decade, this link with the dollar served Asian countries well. It facilitated the long boom in foreign direct investment into the region, with all the associated benefits, including technology transfer, which came with it. From the mid-1980s, Japanese companies built as much manufacturing capacity in continental Asia as exists in France. Businesses borrowed dollars cheaply at low rates of interest, thinking that the fixed tie with the American dollar gave them a natural hedge.

But then the game changed. In the two years after 1995, the US dollar rose 60 per cent against the yen, dragging the pegged Asian currencies up with it. As these economies became less competitive, their current accounts were exposed to much greater scrutiny, especially as regional exports fell after 1996.

The artificiality of the dollar pegs became more obvious, and devaluation became inevitable.

Stephen Grenville, the Deputy Governor of the Reserve Bank of Australia, recently described the crucial combination of elements in the crisis as ‘the large volatile foreign capital flows, plus fragile financial sectors’ which made these economies very vulnerable to changes of confidence.

In effect, the pressures of growth had become too great for the inadequate structures of the Asian countries to cope with. Their economic systems lacked transparency, banks were often seriously under-regulated, lending was politically directed and legal structures were inadequate.

The contagion spread with astonishing speed. In the markets, as the academic Jeffrey Sachs put it: ‘Euphoria turned to panic without missing a beat.’

The economies of Thailand and South Korea, Malaysia, the Philippines and Indonesia came under scrutiny, then pressure.

But nowhere has the pressure been more intense than in Indonesia, and nowhere in Southeast Asia will the consequences be more serious. The reasons this should be so are matters of the greatest importance to Australia.

I said as Prime Minister that no country was more important to Australia than Indonesia. That reality will be brought sharply home to us over the next twelve months.

Clearly, what happens in Indonesia affects Australia's prosperity and security directly. We can't isolate ourselves from the consequences of large-scale economic, social or political uncertainty among the 200 million people living on an archipelago which stretches over 5000 kilometres across our north.

But developments in Indonesia affect Australia indirectly as well, because what happens there will determine—not simply shape or mould but determine—how quickly and peacefully the rest of Southeast Asia can develop.

This was a lesson which was clear to us more than 30 years ago, as Australians and our neighbours in the region watched with relief the transfer of power from President Sukarno to General Soeharto and the establishment of the New Order Government.

It is important to recall that time. Indonesia's economy was in chaos, inflation reached 1000 per cent, and as part of its policy of confrontation against Malaysia, the Indonesian government had launched attacks on its nearest neighbours. Australia was directly, if unofficially, involved in that military conflict.

The consequences of those developments in Indonesia in 1965 and 1966 have shaped Australia's environment for the past 30 years. As I have said before, the coming to power of the New Order Government was the single most beneficial strategic development for Australia in the postwar years.

In abandoning the dangerous international adventurism of his predecessor, President Soeharto provided the solid underpinning for successful regional cooperation through ASEAN and later APEC.

He refocused the efforts of the Indonesian government on economic and social development. The New Order Government delivered consistent economic growth of around 7 per cent a year.

And, just as importantly, the growth was spread widely. According to the World Bank, poverty was reduced more rapidly in Indonesia than in any other country it has studied.

The social indicators were equally strong. Over the past 25 years, the number of Indonesians living in absolute poverty fell from 60 per cent to 11 per cent, infant mortality was halved and life expectancy rose by seventeen years. Literacy rates were up from 39 per cent in 1960 to more than 80 per cent now. Economic modernisation and family-planning successes mean that there are some 50 million fewer Indonesians than would otherwise have been the case.

As a result of these developments, Australia was saved literally billions of dollars in defence expenditure and a market was created for trade worth $A5 billion last year.

Until this current crisis, Indonesia had been one of Asia's great success stories. In addition to a high growth rate, its current account deficit was less than 4 per cent, its budget was in balance and inflation under 10 per cent.

As in Thailand, Indonesia's economic problems began when its government was unable to sustain its informal currency peg between the rupiah and the US dollar. Indonesia had benefited greatly from that peg and the inflow of foreign direct investment it brought. But one of the consequences of opening up the economy was to give the financial and currency markets of New York and London and Frankfurt a significant influence on the Indonesian economy. I don't think this change was fully understood in Jakarta.

As the Indonesian economy came under greater scrutiny, problems everyone had known about—and lived with—like a weak banking sector, a lack of transparency in the economy, and political direction of investment decisions were put under the microscope.

Capital started leaving Indonesia, capital inflow slumped and confidence evaporated in the local market. The problems were magnified because an estimated 75 per cent of the offshore private-sector debt of around $74 billion was unhedged.

As the rupiah came under pressure, the Indonesian government realised it did not have the resources to defend the peg. In August 1997—quite early in the crisis—it decided to float the currency.

But neither that action, nor its extensive economic deregulation package in September, nor an IMF package in November, which the Indonesian government was praised for seeking in a timely way, were sufficient to restore market confidence.

The annual budget delivered in January had some strong points, but was undermined by out-of-date economic assumptions, especially about the value of the currency. The government was forced back to the IMF to negotiate another, even larger, $43 billion, package of support.

This package, which was signed on 15 January, surprised almost all observers with its comprehensiveness. It involved extensive economic restructuring, including fundamental reform of the financial sector, and the dismantling of most government monopolies. 'Sweeping away all the restrictions,' was the way the IMF put it.

But despite these measures, the rupiah has not recovered. From a rate of 2430 to the US dollar in mid-1997, it has dropped to a current level of around 10,000. In these circumstances, Indonesia's high foreign debt of $120 billion becomes an insupportable burden. In essence, the Indonesian government has lost control of the pace of its adjustment to the global economy.

To give some idea of what Indonesia has to cope with, the decline in the rupiah's value is the equivalent of the Australian dollar falling from 75 cents to 10. No government can cope with that. The current rate of exchange is quite unreal: a fiction which bears no relationship to the strengths of the Indonesia economy.

As the Governor of the Reserve Bank of Australia, Ian Macfarlane, has pointed out, ‘Falls of this size defy economic logic and serve no useful economic purpose . . . There is no value to Indonesia, to the region or the world in now having an exchange rate at a quarter of its former level.’

But Indonesia’s economic problems are not confined to the financial sector. In parallel with the currency crisis, the widespread El Niño drought has brought smaller rice harvests and food shortages as well as catastrophic forest fires in East Kalimantan.

This depressed economic outlook, and the impact of many of the IMF reforms, will have serious social consequences. These cannot be avoided.

Fuel subsidies will be cut and food will rise in price. At the same time, the unemployment results of the currency collapse will be felt more strongly. Official estimates, almost certainly too low, are for a 50 per cent increase in the number of unemployed to 6.5 million during the course of the year.

The Indonesian economy is expected to contract by at least 5 per cent this year. And inflation is already rising and is expected to hit 40 per cent. Hyperinflation is possible.

These economic problems raise the likelihood of social unrest. Resentment against Chinese shopkeepers could lead to further looting and rioting with unforeseeable consequences. The leadership of the Indonesian armed forces is strong and competent but, in such circumstances, discipline will be tested.

This is not just a matter of foreign-policy concern. It is a human tragedy. The economic decline has dashed the prospects for tens of millions of ordinary Indonesians, who for the first time had been seeing some real improvements in their lives and better hopes for their children.

Why did it happen? Why have markets punished Indonesia so much more severely than other Asian countries in demonstrably worse macroeconomic shape?

The main reason is that the future of the Indonesian economy became caught up in judgements about its political system.

This was partly unfortunate timing. The onset of the crisis coincided with what was always going to be an uncertain political period in Indonesia leading up to the presidential elections. Markets like certainty and the Indonesian political timetable meant they couldn’t have it.

Aspects of Indonesia’s own response to the crisis contributed to the difficulty. It sent out mixed and sometimes confusing messages—as in the uncertainty about the currency board proposal. And it has backtracked on some important issues in the agreement with the IMF (as well as on some trivial issues which had a symbolic importance internationally).

The regrettable truth is that times like these require directness and clarity rather than Javanese obliqueness.

But most importantly, in my opinion, Indonesia was disproportionately punished because a grossly inaccurate view had taken hold in some quarters in Europe and North America that it was some sort of rogue state, to be talked about in the same breath as Mobutu's Zaire or Marcos's Philippines. Partly as a result of East Timor and a domestic dispute over political fundraising in the United States, Indonesia had become a symbol and a caricature rather than a real, complex and deeply important country.

Indonesia has not been good at telling its own story. It is noticeable how few voices exist in the United States or Europe willing to speak out for Indonesia—I'm not talking about the government here but the country and people.

The result was that the international goals for dealing with the crisis, and the performance measurements against which Indonesia would be judged, were expanded and restructured to include, explicitly, wholesale economic and social reform, and, implicitly, a change in the political leadership.

So the IMF's demands included not just measures to allow orderly economic adjustment but a complete reordering of the Indonesian economy.

It seized the opportunity to try to impose in one sweep an extensive and intrusive program of change. Some of the reforms it demanded were badly needed and will greatly strengthen the Indonesian economy when it recovers. But they have made that recovery more difficult by changing Indonesia's political dynamics and imposing goals which were politically unachievable, and therefore delaying any restoration of confidence.

It is important to remember that despite Indonesia's rapid growth it remains a developing economy with serious problems of administrative efficiency—just in getting the government's writ to run. It ought not be surprising if it has run into difficulty implementing a complex package of reforms which I doubt that Australia, with a smaller population and better communications, could have put in place in two months.

It was noticeable that almost before the ink was dry on the January agreement, prominent voices in the United States and Europe were casting doubts on Indonesia's willingness to comply. This had elements of a self-fulfilling prophecy about it. It undercut, almost immediately, the very confidence the measures were designed to restore.

Some of the commentary we are seeing about Indonesia has a chilling tone to it. Those who argue that the screws should be tightened on President Soeharto and the government because this will somehow force political change show tragically little understanding of what the consequences of widespread unrest in Indonesia would be for real people in the real world.

The IMF has done its job with good intentions, but I agree with those who argue it has been the wrong job. Or perhaps the right job, but in the wrong time and manner.

I am certainly not arguing against further reform. I fully agree with the need for greater transparency and economic and political openness. This is a line I have pressed in APEC and around the region.

The immediate need, however, is to stabilise the rupiah and get it back to a figure around 5000 to the US dollar.

This can’t be done without wholesale reform of the banking and finance sectors, and the satisfactory rescheduling of Indonesia’s corporate debt. But it doesn’t require the immediate dismantling of the clove monopoly, however worthy a goal that might be.

The essential requirement is to get confidence back into the investment community, both domestic and international.

To do this Indonesia has to directly address the question of the private debt owed to overseas creditors. So long as this issue is unresolved, solvency will not be restored to the bulk of the corporate sector and the rupiah will continue to hover at unrealistically low levels.

In part this might be done by the large Indonesian companies converting debt into equity, or at least acknowledging that even at any reasonable exchange rate the corporate debt will still be too high and will require dealing with. A move along these lines would help confidence in the rupiah.

The new government has already announced plans to restructure its 164 state-owned companies and has foreshadowed the development of strategic partnerships with foreign firms. It will find benefits in moving speedily on this front.

The signs over the past few days have been hopeful that sensible dialogue is underway again between the IMF and the new Indonesian government.

Having originally left the central issue of private-sector debt largely to lenders and borrowers, the IMF is now involved in discussions with the Indonesian government on the matter.

And it appears ready to accept that some of its original macroeconomic goals relating to rates of economic growth, inflation and the current-account deficit are unreachable, and that the social impact of some of its demands, like the immediate dismantling of the state-controlled food monopoly and cuts in subsidies to food and medicine, would be too severe.

The two sides also appear to be at least discussing a new way of stabilising the currency by adopting some sort of currency band system.

But even if Indonesia and the IMF reach agreement, under the best circumstances imaginable it will be a long tough road to recovery in Indonesia.

I believe Australian policy through this critical period has to be based on this one fundamental: we stand with Indonesia.

It is the same message the Labor government sent to the young republic during the revolution. We are with Indonesia whatever happens.

Australia cannot insulate itself from the future of the 200 million people who are our nearest Asian neighbours. And we should not try to do so.

I know that the statement ‘We stand with Indonesia’ begs some important questions. Is standing with Indonesia the same thing as standing with the Indonesian government? How exactly do we stand with Indonesia? What are the practical things we can do? What is the crossover point between helpful neighbourliness and counterproductive intrusiveness?

But these are exactly the questions we should be debating.

My point is that if you approach policy formulation from that starting principle you reach different conclusions from those which follow if you begin from other points like ‘How can Australia firewall itself from the impact of what is happening?’ or ‘How can Australia best bring about political and social change in the region?’

Well before I became Prime Minister I was concerned that despite the long efforts of committed people in both countries to build friendship, the relationship between Australia and Indonesia seemed little more than a thin foreign policy veneer. I believed Australia faced serious dangers if it entered the twenty-first century without trying to build a relationship of trust and substance with our nearest Asian neighbour.

Significant misunderstandings persisted in the public mind on both sides. Research we commissioned in 1994 showed that fewer than one in five of the Indonesians surveyed saw Australia as a modern or advanced society, only 2 per cent were aware of Australian manufactures and mining products, and a depressingly large two-thirds believed the White Australia Policy was still in operation.

On Australia’s side, suspicion of Indonesia as a long-term threat to the country persisted. It was fuelled by an equal level of ignorance about modern Indonesian society. Some in Australia believed that geography made Indonesia a permanent threat to this country.

What both President Soeharto and I tried to do was to construct a framework for a relationship which would endure after we had passed from the scene. I certainly valued my friendship with him, but I was also conscious that our friendship would not be enough to change the nature of the relationship. What we had to do was to increase substantially the number of stakeholders in it.

So on my first visit to Jakarta as Prime Minister in 1992 we established a new ministerial forum to meet every two years and to bring together ministers from a whole range of economic and social portfolios. We wanted the different areas of government to discover new opportunities for cooperation.

On the defence side we developed the Agreement on Maintaining Security as an historic declaration of trust between us, a recognition that Australia and Indonesia had common, not conflicting, security interests in the region, and in appropriate circumstances could respond through common measures.

We improved the foundations for trade and economic ties. A major trade promotion in Jakarta in 1994 was attended by the largest number of Australian business people ever to attend a trade fair abroad.

But we also knew this had to be more than a government-to-government relationship.

We worked to build up the number of people outside government with a stake in the relationship, supporting Indonesian-language teaching and setting up the Australia–Indonesia Merdeka Fellowship scheme to bring outstanding Indonesians to Australia and send outstanding Australians in mid-career to Indonesia.

To underpin all this, I made six visits to Indonesia between 1992 and 1995. This was more than the total of all previous visits by Australian Prime Ministers in the preceding twenty years.

None of this was done with short-term politics in mind.

For that reason I was genuinely pleased to hear Indonesia ministers talk with obvious satisfaction about the commitment of their counterparts in the Howard government to the Australia Indonesia Ministerial Forum in October 1996.

But the depth of our accomplishments, and the work of so many other Australians in and out of government over the past 50 years, will be tested in coming months.

In the policy now being developed, our aim has to be what will cause least pain to the Indonesian people and what will get growth going again. Australia’s role is not to stand in judgement over Indonesia, marking boxes with ticks and crosses and awarding points for adherence to IMF packages before deciding whether or not we should respond to Indonesia’s needs.

In this crisis Australia needs to be a miner and distributor of ideas.

This isn’t just a job for government but for business and universities as well—for anyone who can understand and interpret what is going on. Over a period of nearly 50 years, Australian universities, beginning with people like Sir John Crawford and Heinz Arndt, have maintained a level of scholarship on Indonesia which is among the highest in the world. Now is the time for contemporary Indonesia scholars to contribute to the debate.

Australia can’t compete with the large economies in offering multibillion-dollar loans to Indonesia. But we should be a principal coordinator of support and a major deliverer of services and advice in areas like information, education, applied systems and public administration.

We should be substantially increasing our support to enable Indonesian students to continue studying in Australia during this period.

Food will be critical in the months. I think the government has its priorities right in looking to the humanitarian task ahead. But the Labor Party's proposal to broaden this into a mini-Marshall Plan involving not only the World Bank but the FAO and the World Food Program, together with an international coalition of aid donors, deserves the government's support.

This is a regional, not just a national, crisis. Indonesia is the epicentre of Southeast Asia and we need to work as closely as possible with our other neighbours in trying to address the causes and consequences of Indonesia's problems.

I can't tell what will happen in Indonesia over the coming months. But I am much more confident than many. We have been treated to a good deal of coverage—some of it shrill—about what lies ahead, including prophecies of the break-up of the archipelago, or a renewal of the massacres of 1965, or flotillas of refugees fleeing Java.

I can confidently offer advice about what we will not see. Historical analogy is generally a lousy way of predicting the future, and it is especially so in this case.

This is a very different Indonesia from the country of 1965 and 1966.

In the weeks and months ahead, my earnest advice to you is to discard immediately any newspaper articles or television reports you come across which include phrases about Years of Living Dangerously.

In some ways, the political stability over the years of the New Order Government has disguised to the outside world the speed of change in Indonesia since 1966. The country has been transformed from a rural to an industrial economy, from a village to an urban society, from a largely illiterate society to one where education is spread widely. Agriculture made up half the economy in 1966. Now it is around 20 per cent. A large middle class of around 15 million has emerged.

And because of these achievements, Indonesia is no longer the country it was. With its integration into the world economy have come changing expectations about the kind of society it should be.

Formally or informally, issues like the place of pribumi business in the economy, the long-term role of the army and whether it retains its dual functions in the security and political areas, ways of addressing differences in the rates of development between the central and outer islands, and means of getting greater public participation in politics are all being debated in Indonesia.

So change isn't going to stop now. It will continue just as it has continued in other Asian societies, and in our own. But it is change which must come from within.

One great danger is that as the political and social consequences of the economic downturn become clearer, Indonesia and other countries of the region will turn inwards and conclude that engagement with the world was the cause of their problems, rather than the source of their growth. (And it is worth recalling that despite the experience of the past twelve months, Asia in recent years has seen the largest and fastest surge of growth in human history.)

Prime Minister Goh of Singapore has spoken of the danger of a broadening of this sentiment to include a reassessment of the region's relations with the West.

Voices in Asia are now being raised in favour of greater autonomy. This is fine. Asian countries can be as autonomous as they like. But they have to accept that a trade-off exists between autonomy and growth. In a world revolutionised by information technology, autonomy won't deliver enough jobs to absorb the growing number of young job-seekers.

And the domestic savings on which these economies have depended will no longer be sufficient. They will continue to need access to international financial markets and to the technology and expertise which foreign direct investment can provide.

Asia does not have to play according to the Authorised Economic Version or the Wall Street Model. There are obvious cultural dimensions to the way Asian economies work, just as there are to the American or German or Australian economies.

But Asia does have to play by the rules which facilitate growth.

You can't attract investment without an economic rate of return and you can't get the best sort of investment without providing the opportunity to litigate your interests. The challenge for these countries is to find ways of preserving their cultural autonomy and the different social, and inevitably financial, obligations which accompany it while improving transparency.

If this danger of an inward-looking Asia is to be avoided, the best antidote to it will come through the policy prescriptions and examples of the regional great powers—Japan, China and the United States.

In particular, the speed with which Asia emerges from recession and the longer-term strategic impact of the crisis will depend on whether Japan can stimulate its economy and use it to drive growth elsewhere; China can cope with its huge domestic challenges and withstand the strong pressures it will face to devalue its own currency; and the US economy continues to grow and to remain open to Asian exports.

Japan's response to this crisis so far has been deeply disappointing. The original victim of the Asian economic crisis, it is still mired in a long structural recession.

It is likely to see negative growth this year. At the same time, its trade surplus rose 88 per cent in February over the same month a year ago. And its imports were down from every Asian country.

One of the most effective ways through Asia's current problems would be for Japan to resume its role as the regional engine of growth and expand its capacity to absorb some of its neighbours' exports.

Japan has generously contributed to the IMF packages and Prime Minister Hashimoto has been personally involved in the problems of Indonesia. But what has been absent is much of a sense of Japan taking a leadership role in the region, generating ideas, marshalling support and making decisions about its own economy in full cognisance of their impact on its neighbours.

When we look back at this crisis in coming years, I believe the thing for which it will be remembered is not that Asian economic growth suddenly stumbled. That was always going to happen in one form or another. The historically significant thing about it will be the way China handled the first region-wide crisis since it reasserted its role as a great power.

China's neighbours have been looking carefully at the way it responds to these current difficulties as a measure of the way it will behave in future, as a test of the sort of power it will be.

By any measure, the results so far have been encouraging.

Although the massive devaluations of other Asian currencies will impose new pressures on China's exports, cutting its growth rate back to under 8 per cent, the government has promised to avoid any competitive devaluation of the yuan. It has justified this decision precisely in terms of the harmful impact such action would have on its neighbours.

China has instead adopted a policy of expanding domestic consumption. It has begun a public-works program equal to 1 per cent of economic output.

But just as important has been the example China has provided. It has demonstrated that the best way out of the crisis is by continuing bold reform rather than retreating into introspection and caution.

It has taken on the huge challenges of reforming the state-owned enterprises and the banking system. It has begun the largest restructuring of the machinery of government since 1949. It has signalled new measures to encourage foreign investment in China's infrastructure. On the political front it has announced that it will sign the International Covenant on Civil and Political Rights.

No-one, least of all President Jiang or Premier Zhu, would underestimate the huge difficulties of keeping reform and growth going in an economy of 1.2 billion people, but China's handling of its response to this crisis suggests that it is conscious of the responsibilities of leadership and capable of acting beyond narrowly defined national interests.

The United States has now had a period of prolonged economic growth, from the first cycle of investment associated with the digital economy—beginning in 1992. This has been fed by a stockmarket which can shift capital effectively and efficiently out of unproductive sectors into productive sectors. With luck, the Asian crisis will help the United States continue to grow by feeding in deflationary effects.

However, virtually all the Asian economies will be basing their strategies for economic recovery on even more competitive exports. And the United States market is the one they will be looking to.

But the United States foreign-trade deficit for the last three months of 1997 was already the highest ever recorded and seems set to grow. A further surge of Asian imports will fuel protectionist sentiments in Congress. This will be happening at a difficult point in the electoral cycle.

Although the administration has been heavily involved in seeking solutions to the current economic crisis, it is hard in the post-Cold War United States to find congressional or public acknowledgement of the link between American prosperity and the rest of the world, or indeed much interest in the outside world at all. The forces standing in favour of a confident United States multilateralism seem to be losing ground.

A growing problem for the rest of us is that the cost to the United States administration of securing US public and congressional support for international issues like United Nations funding or the current IMF replenishment is increased demands that these organisations demonstrate that they serve specific American goals and ideals. This situation is untenable over the long term for both the United States and the international community.

It was openness and links across the Pacific which delivered Asia’s enormous growth. This crisis has demonstrated yet again how central those trans-Pacific links are. But they require careful tending on both sides of the ocean.

Asian economies are looking at a lengthy and painful period of adjustment. It took Australia about five years to fully exploit its new competitiveness in the 1980s. We turned a huge nominal depreciation of the exchange rate in 1985–86 into a real depreciation. That is, we captured the competitiveness.

But we didn’t start really seeing the longer-term results in our export performance and our import replacement performance until about four or five years later—in 1990. But I believe that the adjustment time in Asia will be shorter because the voices of so many people looking for better lives for themselves and their families won’t be denied.

The underlying factors underpinning Asian growth have not changed: young demographics, high savings rates, sensible macroeconomic policies, entrepreneurial cultures, the high value placed on education.

And if regional governments can get through this immediate period and take advantage of the reforms now being imposed on them, and the competitiveness benefits which the devaluations provide, they will have tremendous horsepower for the next stage of economic growth. The IMF may not have all the answers, but it has provided governments with the authority to make reforms which they could not have drawn down from their own political system.

But the long-term problems for Asia haven't gone away. In a sense, the real Asian economic crisis is still out there, waiting.

This is the crisis of funding and building the infrastructure required to support more than two billion people, to feed and educate them and deal with the profound environmental consequences of that growth.

Asia's energy demand is doubling every twelve years with all the consequences that has for air quality and global warming.

In the early 1990s, around 500 million East Asians lived in towns. By 2020 this figure will have trebled to 1.5 billion. This demographic shift from the countryside to the cities will put a huge strain on basic services like water, sanitation and shelter. Only half the urban populations in developing Asian countries currently have access to safe water supplies and 42 per cent to sanitation.

Food is a looming issue, too. We are already seeing across the region the consequences of unconstrained heavy use of fertilisers, irrigation and pesticides. Agricultural productivity is better, but at the expense of soil erosion, salinity and the pollution of water resources. How will the region supply itself with food without destroying the land for future generations?

These looming problems have largely been forgotten in the current turmoil. But they will require even greater attention once the current crisis has passed.

Unfortunately, as we have seen over the months since last July, global and regional organisations are nowhere near ready to respond effectively to the new challenges of globalisation, and the changes it is bringing to the international system.

Throughout this past year, the principal institutions we might have looked to for help have been out of breath, or behind the play, or playing the wrong game.

Many writers have commented, and all of us know intuitively anyway, that the pace of global change is quickening. It is still fewer than ten years since the Soviet Union collapsed, and with it the whole postwar international order. Now, only a few years later, we are seeing an economic crisis in Asia that threatens to hobble the region which had promised to be the world's economic growth engine as we enter the twenty-first century.

History is made up of discontinuities. But surely one of the main lessons of the past decade is that those discontinuities are becoming more frequent and deeper.

In other words, it is not the speed of change which should concern us most, but the fact that change seems to be becoming inherently more sudden and less predictable.

The reason lies in the profound impact on the international system of the information revolution in all its various forms, including the way it has made economic globalisation possible and has accelerated the mobility of capital, information and ideas.

The Asian economic crisis has been an obvious example of this.

We are likely to have less warning of future crises and therefore fewer opportunities to avert them. And when they come, the swings they generate are likely to be larger. We do not as yet fully understand the new system’s dynamic and that we need to update and modify our institutions and practices to reduce the risks inherent in it.

The IMF has had a lead role in this crisis, but it is a very different, much broader, role than the sort of balance-of-payments crises it has had to contend with in the past. The officers of national finance ministries which make up and run the IMF haven’t been able to assimilate properly the political dimensions of the new job they are now being asked to perform.

The momentum for changes to the processes and policies of the IMF is now probably unstoppable.

The G7 has had a go at thinking about the crisis, but its problem in these circumstance is that the interests of its European members demonstrably don’t extend to the political stability of Southeast Asia.

APEC ought to have been ideally placed to respond to the region’s difficulties because it is an economic organisation which includes all the countries most affected.

One problem which has clearly emerged has been the absence of a strong APEC secretariat with institutional backing able to bring issues and current data to the attention of member economies.

But more basically, APEC has been hobbled by the agreement last year to add Russia to its membership.

I think this decision was an act of international vandalism. I would have opposed it to the end. It was a fundamental mistake which was made worse because it was designed in part to atone for another fundamental mistake: the 1997 decision to expand NATO to the European borders of the old Soviet Union.

I’m certainly not anti-Russian and I well understand its long-term importance as a great power. But its participation in APEC has already changed the dynamics of the organisation.

Under no conceivable stretch of the imagination is Russia currently part of the Asia Pacific economy. And its strategic and political priorities are totally different from those of APEC’s other members.

Precisely because it is such an important power in its own right, its participation will make it harder to use APEC and the Leaders' Meetings as a focused and effective forum to oversee and coordinate the various responses to the economic crisis. Russian membership makes it impossible, for example, to contemplate using APEC as the basis for a financial fund to address future balance-of-payments problems in the region, because the potential additional demands it would generate are just too great.

The Declaration which emerged from the Leaders' Meeting in Vancouver last November described APEC as the 'region's most comprehensive economic forum' and 'particularly well placed to play a pivotal role in fostering dialogue and cooperation'. It asked APEC finance ministers and central bankers to accelerate their work. It talked about an increasing role for APEC.

Well, we haven't been swept aside in the rush.

This year's APEC meeting in Kuala Lumpur has to send firm messages that Asia remains on the path to openness. This isn't just a matter of making declarations but of taking specific actions which will restore confidence within the region and in key markets that Asia can resume its growth path.

This means showing a determination to move forward on the Bogor free trade and investment agenda.

It means giving some clear support to the development of more structured cooperation between regional central banks.

But if APEC is to get anywhere, the bulk of the work to achieve it has to be going on now. It will be useless for leaders simply to turn up in Kuala Lumpur in September and expect to put something together in those couple of days.

I'm not prepared to write APEC off yet. But if it doesn't show its relevance to the Asian economies this year it will write itself off.

What happens to any individual international organisation isn't in the least important.

But APEC matters because it embodies a big idea—that of an open Asia Pacific region. And that idea lies at the core of how we can best overcome this mess.

On the trade front, the message has to be sent out strongly that the world is not in the business of building barriers. We need China in the WTO, and as quickly as possible. I hope this will be one of the outcomes of President Clinton's proposed visits to China in June.

More broadly, this would be an excellent moment to press ahead with the proposed Millennium Round of trade negotiations.

Let me end by returning to the subject of Australia and Asia.

I believe the changes Australia made internally in the 1980s and 1990s have prepared us well to cope with the challenges we now face. We went voluntarily through much of the painful integration into the global economy that our neighbours are experiencing.

I also believe the progress we have made in forging closer bilateral and regional ties will help both Australia and the countries around us.

But I have to note that a few worrying signs about Australia's relationship with Asia are emerging.

For example, I was taken to task by the *Sydney Morning Herald* last week.

This is not a new phenomenon, of course, or one which strikes fear in the heart. But it is worth mentioning because the criticism has broader implications.

I was criticised for a speech I made in Singapore in 1996, from which the editorial quoted. I had said that Australia's 'engagement with the region around us is not just commercial. And it is not just the result of some crude economic determinism. It goes—and must go—much deeper than that. It goes to a genuine desire for partnership and real involvement . . . Australia needs to seek its security in Asia rather than from Asia'.

This view was described by the newspaper as 'light-headed'.

But to assert, as those words of mine do, that Australia's engagement with Asia has a political, security and cultural dimension as well as an economic one, and requires a genuine national commitment on our part, seems to me so deeply true, so basic to Australian interests, so blindingly self-evident, that it is perhaps only a *Sydney Morning Herald* editorialist who could take exception to it.

But unfortunately there are other hints of revisionism around. A sort of *sotto voce* whisper that the Labor government rather overdid the whole Asia thing and that we are now paying the price. Some of the old brigade obviously think Asia's recent economic problems mean that Australia can heave a sigh of relief and head for the safety of old friends and familiar geography.

Others argue that some historically determined conflagration is coming in Indonesia and that Australia should distance itself from it by tiptoeing quietly to the side of the field in the hope that no-one will notice we are there.

This is dangerous nonsense.

Australia must have a deep and continuous commitment to Asia— and for reasons that lie at the heart of our national interests. None of that has changed as a result of recent developments.

The intrinsic economic complementarities between Australia and Asia have not changed. Australia has not suddenly developed security interests in Africa rather than Asia.

Australian engagement with Asia is not a temporary enthusiasm. Asia is not a flavour of the month. We have not been on a ten-day package tour from which we can return with a couple of T-shirts and a handful of colour prints for the album. Australia can't bolt on the Evinrude and motor off to the coast of California.

If we know anything about dealing with Asia it is the importance of building relationships for the long term.

That's the business Australia needs to be in now.