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A Recapitulation of Asian Financial Crisis and Institutional Factors

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บทคัดย่อ

วิกฤตการณ์ทางการเงินปี 2540 ซึ่งถูกประทับตราไว้ในประวัติศาสตร์เศรษฐกิจของเอเชียนั้น ได้ก่อให้เกิดความพยายามในหมู่นักทฤษฎีและนักปฏิบัติที่จะอธิบายเหตุการณ์ที่เกิดขึ้น ความคิดในขั้วหนึ่งเห็นว่าปัจจัยที่เป็นจำเลยได้แก่ การแทรกแซงที่ผิดพลาดโดยรัฐบาลที่ก่อให้เกิดความไร้ประสิทธิภาพ ขาดความโปร่งใส การฉกฉวยประโยชน์จากกฎเกณฑ์ที่ไม่ชัดเจนรัดกุม การแสวงหาค่าเช่าทางเศรษฐกิจ และกรณีที่เลวร้ายที่สุดคือ การฉ้อราษฎร์บังหลวง ส่วนความคิดเห็นในอีกด้านหนึ่งกลับมองว่า วิกฤตเป็นผลพวงที่ไม่อาจหลีกเลี่ยงได้ของการเปิดเสรีที่ไม่ระมัดระวังและทะเยอทะยานเกินไป รวมทั้งการแปรรูปรัฐวิสาหกิจที่ผิดจังหวะเวลา ความเห็นในกรณีหลังนี้มีแนวโน้มที่จะเห็นด้วยกับรัฐที่มีบทบาทเชิงรุกในระบบเศรษฐกิจ

การรวมเอาทัศนะทั้งสองด้านเข้าด้วยกันและยอมรับให้รัฐยังมีบทบาทในการทำงานของระบบเศรษฐกิจ ก็เท่ากับยอมรับว่า สภาวการณ์ของ "ธรรมาภิบาลที่ดี" ยังไม่อุบัติขึ้น เมื่อเราได้พิจารณาอย่างลึกซึ้งยิ่งขึ้นก็มิอาจปฏิเสธได้ว่า ปัจจัยที่เป็นจำเลยในทัศนะทั้งสอง ไม่ว่าจะเป็นการแทรกแซงที่ผิดพลาดของรัฐ หรือการเปิดเสรีที่ทะเยอทะยานเกินไป ล้วนเพียงแต่ทำให้วิกฤตเลวร้ายลงและยืดเยื้อออกไปเท่านั้น แต่เราอาจสงสัยและถามว่า ปัจจัยเหล่านี้เป็นรากเหง้าที่แท้จริงของวิกฤตหรือไม่ เพราะหากปัจจัยเหล่านี้เป็นรากเหง้าของปัญหาจริงแล้ว ปัจจัยเหล่านี้ก็ไม่ควรจะมีปรากฏอยู่ในช่วงอื่นก่อนเกิดวิกฤต แต่กลับเป็นที่ชัดแจ้งว่า ตั้งแต่ช่วงเจริญรุ่งเรืองทางเศรษฐกิจก่อนเกิดวิกฤต ระบบเศรษฐกิจดังเช่น ประเทศไทย และประเทศในเอเชียอื่น ๆ

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ก็ล้วนมีส่วนผสมของององค์ประกอบเหล่านี้อยู่แล้ว ทั้งการแทรกแซงที่ผิดพลาดของรัฐบาลและการเปิดเสรีที่ทะเยอทะยานเกินไป ซึ่งนำมาสู่ระบบที่เรียกว่า "ทุนนิยมอุปถัมป์" อย่างหลีกเลี่ยงไม่ได้

หากเราต้องการที่จะตอบคำถามที่ว่า ปัจจัยเหล่านี้เป็นรากเหง้าที่แท้จริงของวิกฤตหรือไม่ เราก็จะต้องก้าวให้พ้นคำอธิบายในแง่ "ความล้มเหลวทางนโยบาย" ไปสู่การประเมินความอ่อนแอทางการเมืองและทางสถาบันในประเทศเอเชียเหล่านี้เสียใหม่ บทความนี้มุ่งที่จะทบทวนบทบาทของการเมือง ซึ่งได้แก่ องค์ประกอบและปฏิสัมพันธ์ระหว่างกัน ซึ่งเป็นแกนกลางสำคัญอันหนึ่งที่ส่งอิทธิพลต่อการเกิดและการทำงานของสถาบันหลักของประเทศ ต่อการก่อรูปและ/หรือเบี่ยงเบนทิศทางของการวางนโยบาย ไม่ว่า นโยบายนั้นจะมุ่งแทรกแซงระบบเศรษฐกิจหรือเพื่อเปิดเสรี

Abstract

Asian financial crisis, a remarkable imprint on the history of the Asian economy for more than half a decade since, has inspired various generic explanations amongst theorists and practitioners. At one end of the spectrum, the "culprit" factor points to the misguided interventionism that created inefficiency, lack of transparency, moral hazard, rent-seeking and, to the worst case, corruption. The other streamline of opinion, however, views the crisis as the inevitable outcome of non-conservative and ambitious liberalisation and untimely privatisation. This is a view more in favour of an activist state.

Recapitulating the two views, and accepting that the state has a place in the functioning of the economy, is equivalent to saying that the status of the ideal "good governance" has not yet been attained. Given a more in-depth reconsideration, one cannot simply deny that the culprit factors in either of the two views, whether be it the misguided interventionism or the ambitious liberalisation, merely exacerbated and prolonged the crisis. Nonetheless, one might be doubtful to ask the question: Were these factors the *actual* roots of the crisis? If they were, then they must have never been present or significant at any other period of time prior to the crisis. However, it is apparent in an economy such as Thailand and many Asian countries, throughout the period of pre-crisis impressive economic performance, have well been composed of the mixture elements of both the

interventionist and market-led policies. This inevitably bred some degrees of the so-called "crony capitalism".

Should one be so inclined to answer the question: "Were these factors the actual roots of the crisis?" then a step *beyond* the explanation of 'policy failure' requires further reassessment of the political and institutional weaknesses in the Asian countries. That is to say, this article reviews the role of politics (that is, its "composition and chemistry"), one of the important vertebrae axes influencing the making and the working of the country's major institutions, in shaping and/or deflecting the direction of the policy design, whether be it the pro-interventionist or the pro-liberalist.

1. Introduction

It was just until after a decade from the mid-1980's that Asia attracted half of the total capital inflows to developing countries. What is known today as the "Asian financial crisis" was the July 1997 financial crisis that originated in Thailand. By the end of 1996, large external deficits accompanied by tremendous external borrowings excessively exposed the country to foreign exchange risk in both the financial and corporate sectors. In short time, the effects spread to affect currencies, stock markets and other asset prices of several Asian countries, many being a part of the East Asian Tigers.

Asian financial crisis, a remarkable imprint on the history of the Asian economy for more than half a decade since, has inspired various generic explanations amongst theorists and practitioners. At one end of the spectrum, the "culprit" factor points to the misguided interventionism that created inefficiency, lack of transparency, moral hazard, rent-seeking and, to the worse case, corruption. The other streamline of opinion, however, views the crisis as the inevitable outcome of non-conservative and ambitious liberalisation and untimely privatisation whilst the pre-crisis conditions prevailed urgent attention of the state to the provision of infrastructure and basic services, coverage of education and health care, unemployment, income distribution and poverty. This is a view more in favour of an activist state.

Recapitulating the two views, and accepting that the state has a place in the functioning of the economy, is equivalent to saying that the status of the ideal "good governance" has yet been attained. What, then, are the requirements for a "good governance"? Standard governance guidebooks would list the required qualifications to good governance as these: a reduction of unwanted government intrusion, an increase in bureaucratic efficiency, a reduction of unnecessary regulation, a greater accountability to the citizens, and an appropriate degree of independence for each government unit. These requirements have the implicit message that good governance is not measured only in terms of the success of the country's economic performance but also in terms of the democratic accountability and participation of the citizens.

Given a more in-depth reconsideration, one cannot simply deny that the culprit factors in either of the two views, whether be it the misguided interventionist explanation or the ambitious liberalisation explanation, merely exacerbated and prolonged the crisis. Nonetheless, one might be doubtful to ask the question: Were these factors the *actual* roots of the crisis? If they were, then they must have never been present or significant at any other period of time prior to the crisis. However, as widely evident in the Asian region, both the interventionist and the (partial) liberalism[2] policies have, for some time, co-existed along with the countries' peak economic performance. Thailand's economy, for example, under a mixture of interventionist and market-led policies (which, unavoidably, breeds some degree of the so-called "crony capitalism"), grew at an average of impressive 9% during 1985 to 1995 and its average real gross domestic product (GDP) grew by 8-13%, standing as one of the fastest growth rates in the world.

If one were inclined to answer 'no' to the question: "Were these factors the actual roots of the crisis?" in the previous paragraph, then a step *beyond* the explanation of 'policy failure' requires further reassessment of the political and institutional weaknesses in some of

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[2] *Partial* liberalisation refers to the situation at which certain selected group of sectors in the economy is being liberalised at the discretion of the state whilst the others remain under the supervision of the public authority and are subject to more rigid controls.

the countries. That is to say, this article reviews the role of politics, one of the important skeletal axes influencing the making and the working of the country's major institutions, in shaping (and/or deflecting) the direction of the policy design, whether be it the pro-interventionist or the pro-liberalist.

2. Tracing the Contagion Effects: An Overview

A macro-scenario reveals that Thailand, Indonesia and South Korea were mostly affected by the Asian financial crisis. From 1985 to 2 July 1997, the Thai baht was pegged at 25 to a dollar. Earlier signs in 1996 can be seen from the American hedge fund already sold US$ 400 million of the baht. On 14-15 May 1997, the baht faced speculative attacks. The, then, Prime Minister, Chavalit Yongchaiyudh initially announced that baht would not be devalued; but eventually Thailand's administration floated the local currency on 2 July. In the following month, in South Korea, which was the eleventh largest economy in the world, its third largest automobile manufacturer, Kia Motors requested for emergency loans. As Moody's downgraded South Korea's credit rating, the country's stock markets faced a sharp fall by an average of 7%.

Indonesia, at the time, seemed far from crisis as it has low inflation, a trade surplus of more than US$ 900 million, high foreign reserves of more than US$ 20 billion and a good banking sector. However, in July, Indonesia began widening its managed currency band from 8% to 12%. Unexpectedly, the Indonesian rupiah came under severe attack in the following month. Following the path similar to that of Thailand, the managed float exchange system was replaced by free-float exchange arrangement on 14 August. Despite the IMF's assistance with a rescue package of US$ 23 billion, rupiah dropped further continuously that Moody's had downgraded Indonesia's long-term debt to junk bond. The intensity of the inflation of the rupiah and the resulting rise in the prices of food stales became apparent in the riots throughout the country.

In comparison to Thailand, Indonesia and Thailand, countries like Malaysia, the Philippines and Hong Kong were relatively less severely affected. Nevertheless, the contagion effects were remarkable. Malaysia at the time was facing a large current account deficit of over 6% of GDP. In July, Malaysian ringgit was also attacked by speculators and eventually the currency had to be floated on 17 August. In response to Standard and Poor's downgrading of the debt rating in Malaysia, Prime Minister Mahathir bin Mohamad introduced capital control measures. However, when he further announced a 10 billion ringgit spending on road, rail and pipeline project, the currency collapsed again. Generally, the outcome in 1998 was that the output in most sectors declined, causing the GDP to fall by 6.2%. Turning to the Philippines early in July of the same year, its central bank intervened heavily mostly by raising interest rate by 1.75%, and then 2% as well as raising the overnight rate from 15% to 24%. The monetary authorities in Hong Kong reacted in similar manners as the other neighbours through spending more than US$ 1billion to defend the local currency. Hang Seng Index dropped by 23%. In addition, on 15 August, it raised the overnight rates from 8% to 23%.

When considering Mainland China (the People's Republic of China), Taiwan and Japan, the first two were relatively unaffected; whereas Japan was undergoing its own prolonged economic difficulties by the crisis time. Mainland China was generally not affected by the crisis because of the non-convertibility of the renminbi (RMB) and because most of its foreign investors took the form of factories on the ground rather than on securities. Despite the fact that China had and continues to have severe solvency problems in their banking system, most deposits were domestic and there was at the time, no urgent liquidity problem. As for Japan, the economy did not collapse completely but was severely hit. Japan was affected due to its economic prominence in the region as countries usually run a trade deficit with Japan. Additionally, the size of the rest of Asia altogether is more than twice that of Japan. Therefore, approximately 40% of Japan's exports go to Asia. Being partly affected by the contagion effects, the real GDP growth rate in Japan fell from 5% to 1.6% and the country eventually went into recession in 1998. There was also a decline in consumer and spending confidence.

3. The Groundwork-building towards 1997 in Thailand

In fact, earlier warning signals of the difficulties in the real sector were hinted in Thailand. Though during the period mid-1980-1995, Thailand enjoyed impressive growth, there were signs that labour costs were rising in comparison with its neighbour countries in the Indochina. In retrospect, Japan had earlier experienced this rising cost of labour in 1960's. Hence, the country had to turn to the relatively more capital-intensive industries. Anticipating a similar pattern of input cost rising structure, Thailand initiated a joint co-operation with its neighbours in the early 1990's. The Bangkok International Banking Facility (BIBF) was due to facilitate specialisation in financing growth in the Indochina. As a preliminary in setting up the BIBF, however, Thailand must liberalise its financial and capital market. Hence, it is evidenced that Thailand increasingly eliminated its interest rate ceilings starting from June 1989 to 1992. In 1990, all current account foreign exchange transactions were liberalised and capital account restrictions were relaxed (Wibulsawasdi, 1995). Having laid the preliminary groundwork, the BIBF was officially opened in 1993. By December 1995, all 15 domestic banks and 30 foreign banks had been licensed by the BIBF.

4. Yew's "Asian-Style Democracy" and Thailand's *Part* Liberalisation

The pre-1997 economic success led many Asian political leaders, the prominent one of which was the Singapore's Senior Minister Lee Kuan Yew, to be in favour of the "Asian-style democracy" (Zakaria, 1994; Goh, 1994). The debate remains unrested as to how self-interested leaders are capable of fairly weighing between the long-run good "deeds" for the country versus their short-run political temptations. Existing cross-national empirical works barely reach solidly conclusive results. For instance, Barro's (1996) finding shows that laissez-faire and democracies perform less well; and Przeworski and Limongi (1993) and Helliwell (1994) show no significant relationship between economic performance and regimes. On the other hand, Devarajan and Lindenberg (1993) and Clague et al (1997) reveal that democracy performs much better. Lacking the unanimous finding to support or reject the "Asian-style democracy," observation reveals that the argument for authoritarianism holds in the newly industrialised nations in East Asia (Haggard, 1990). For instance, Hong Kong, until 1997, was a no-party administrative government under British rule. In Korea, it was the military that took office followed by the restricted democratic rule under Park Chung Hee after 1964. How, then, could the success of the miracles be explained from the observations if laissez-faire were believed to bring greater efficiency? Mancur Olson (1993) asserts that an authoritarian leadership who is far-sighted enough, even though may be self-interested, would create a policy design for the "good" of the country in order to maximise his long-term gains.

It is now to turn to consider the extent of laissez-faire undertakings in Thailand. Until early 1996, Thailand was successful in keeping the baht at the value of 25 per US dollar at the cost of relatively high interest rate. Strictly re-defining, this scenario can only be accepted as a *part* liberalisation, not a true complete liberalisation idealised in the free-market context. With its relatively high interest rates, the *Bangkok Post* headline "Cutting out-in loans by BIBFs not easy," (*Bangkok Post,* 16 January 1997) reported inflows of short-term foreign capital greater than the Bank of Thailand's desired level. This reduces the spread between the maximum lending rates and deposit rates at commercial banks from 7.25% in June 1992 to 4.1% in June 1995. Only the domestic banks can easily acquire foreign funds at an interest rate of 4 to 5% lower than domestic funds. This caused the spread between commercial banks' lending rates and their cost of funds to increase from 2.87% in late 1989 to 3.22% in late 1995 (Wibulsawasdi, 1995).

Nevertheless, the partiality in Thailand's liberalisation attempts must not be overlooked. In contrast to domestic banks being accessible to foreign funds, the Thai finance and securities companies, under a different set of legislation from the banks, have no access to foreign capitals. In other words, the players in the country's financial sector were on an uneven ground. This is clearly apparent from an instance that Thailand's 15 banks had a total of 3,000 branches but the 91 finance and securities companies cannot open branches. Banks can offer different types of deposits; whereas finance companies can only issue promissory notes. Furthermore, since banks normally offer lower interest rates to borrowers, it was only those turned down by the banks who will go to finance and securities companies, facing a riskier portfolio.

Having pointed out Thailand's part liberalisation regime, it may, at this point, be possible to revisit Olson's assertion of the long-term view of the far-sighted leadership. It is now to continue on to the next question: How can we find the political roots of the crisis given this scenario for the case of Thailand? Was a relatively more democratised Thailand affected by the political factors that cause market uncertainty? To some extent, yes, the system allows the public to vote the failed government out of office, as evidenced that Prime Minister Chavalit Yongchaiyudh had to resign in November 1997. However, the democratic government has no strong depth on the extent of the nation's crisis.

With political constraints, policy making in democracy is seriously subject to unity in the government. Therefore, the leader must enjoy a legislative majority or support from a majority coalition. Recalling the case of Korea for an example. In 1997, President Kim Young Sam of Korea enjoyed a legislative majority, but his administration fell victim to divisions within the party and between the executive and the legislature. The internal battles also influenced the management of important corporate failures, notably the Kia bankruptcy mentioned earlier in this article. A picture not so much different in Thailand's constitutional and electoral system, until revised in the late 1997, there had always been serious setback in policy making. This is because the Prime Minister, as a head of government coalition has, throughout the history of coalition governments, been consistently threatened by the coalition partners defect in pursuit of better deals in another coalition.

5. The Moral Hazard Issues

It has now been hinted that the root of the problem arises from the *composition* and the *chemistry* of the Thai administration, and not entirely from the chosen policy design. The composition comprises of the parliamentary structure (because the past governments rest on party cohesion) and a multi-member electoral system (which undermined party cohesion). By having this system, it is likely that there would lack unity in the same party. Hicken (1998) asserts that this would yield selective benefits to voters in the electorate in order to differentiate themselves from rivals of the same party. Thus, this places a high premium on politicians to generate cash flows to the parties to cover the costs.

Once in office, rival politicians are likely to create institutional problems in a way that accumulates economic distortions. The incidence points to relate part of the story to the governing business- government relations, particularly close political relationships between politicians and business constituencies. Nevertheless, there can be optimistic views arising from such a relationship. According to Peter Evans (1995), it is because of the close business-government relations that have been the important features of the Asian model contributing to the region's growth, as he expresses "effective government business relations depended on large quantities of high quality information flowing between government and corporations and on mutual confidence that predictions and commitments were credible".

Observed anywhere else in transitional economies such as Russian Federation and countries in Eastern Europe, once there is a close business-government relationship, the issue of "cronyism" and corruption becomes prominent. However, cronyism and corruption pose more adverse effects than ineffective policy direction in the sense that exchange relationship between business and government in the case of the first two completely ignores any social welfare rationale. Favours were fully passed out to political allies. Although ineffective policy direction, such as misguided interventionist or over-ambitious liberalism, in absence of cronyism and corruption, may as well lead to unfavourable economic performance, there are traces of welfare concerns and some equity touch. An empirical evidence by Mauro (1995) proves the negative correlation between corruption and economic growth over the long run.

Other commentators point down to the policy level, which more directly affects not only the crony "circle of friends", but also the citizens at all levels. They suggest that the close government-business ties could lead to the misguided industrial policy, which favour well-connected firms who could socialise risk or gain access to subsidies, preferential credits, protections and the like through political process. By doing so, the type of government intervention created moral hazard: excessive risk-taking, inefficient allocation of capital and weakening of domestic financial institutions. Weaknesses in financial system, in effect, led to the wider economic crises that ensued. For instance, the case of Korea, reported in *The Economist* (November 15, 1997), that the industrial policy peaked during the Heavy and Chemical Industry Plan of the late 1970s and was gradually dismantled over the 1980s and 1990s as the country liberalised. This shows that prior to the liberalisation, interests were concentrated on certain groups in connection with the heavy and chemical industry. On the other hand, Hill (1995), suggests that the effort of Indonesian government like state-owned steel company, national car project and light aircraft industries played no role in the crisis. The case of Malaysia is more complex as it had long maintained the pro-bumiputra policy (Gomez and Jomo 1997), where procedures for letting government contracts and privatisation have not always been transparent, contributing to the political crisis of 1998 (Jomo, 1998).

In Thailand, corruption, or politically-motivated decision-making, also appears to have played a role in expanding commercial bank sector. Licenses were granted to unsolicited institutions irrespective of their capacity to manage risk. Phongpaichit and Piriyarangsan (1994) document a record of the political manipulation of the budget and budget-related scandals in 1990's. It is to be noted, however, that fiscal management was not the central cause of the crisis, at least amongst the commentators. The roots of the crisis can be more reflected by the failure to regulate and act aggressively against a number of failing finance companies, the extraordinarily costly efforts to save a number of financial institutions and high degree of uncertainty about the government's' intentions.

The high degree of uncertainty about the government's intentions was consistently observed in the common news headlines during the time. In the *Bangkok Post: Year-End Economic Review 1996,* the headline "Greed reaps grim reward" reveals a threatening figure of 755,000 housing units built in Bangkok during 1992 to 1996, whilst the needed were estimated to be only 382,240 units in the seventh National Economic and Social Development Plan. As the 40.4% figure calculated by the Government Housing Bank of the houses remain unoccupied, real estate developers had problems repaying their loans. Banks were supposedly in a superior position than finance and securities companies and, hence, less vulnerable to the speculative bubble in the property market because the property credit only accounted for 8.8% of commercial bank total credits but the non-performing loans were 24.4% of the finance companies' total credits. (Vajragupta and Vichyanond, 1998).

Having higher proportion of non-performing loans as well its status in competing on an uneven ground with banks, finance and securities companies eventually went bankrupt. In February 1997, rumours spread that Finance One, Thailand's largest finance company, had serious liquidity problems due to serious losses on property and equity investments. Yet, here, there is a question of why many banks were severely affected by the situation, too. It was then inescapably revealed that Thailand's financial market had not been separated between banks and finance and securities companies. Many banks had strong connections to its finance and securities companies. However, it was officially unknown how much of the foreign capital inflow was channelled through banks into the finance and securities companies connected. The consequence reveals strong linkage, as it became obvious that information flows led depositors to 'herd' frightening effects to withdraw money to the institutions they felt less risk. In 1997, at the beginning of the year to the month of October, deposits fell by 35.3% at Bangkok Metropolitan Bank, 18.73% at Laem Thong Bank, 11.16% at First Bangkok City Bank, 10.82% at Bangkok Bank of Commerce and 6.2% at Siam City Bank. These banks were considered small and new banks. In contrast, for the bigger banks, deposits increased by 34.16% at Siam Commercial Banks, 22.16% at Thai Military Bank and 19.07% at Bangkok Bank.

On 3 March 1997, the Thai government suspended all trading conducted by the bank and finance companies and required higher reserve requirements ("Market freeze shakes investors", *Bangkok Post,* 4 March 1997). This resulted in an approximately 40% loss in total deposits in finance and securities companies ("Withdrawals slow further to Bht 4 Billion", *Bangkok Post,* 8 March 1997; "Shape up or ship out, says Amnuay," *Bangkok Post,* 9 March 1997). The high interest rates make it worse because more borrowers were not able to meet the obligations of their lenders.

6. Policy Dilemma in Thailand: Democracy works its way

By close to mid-1997, the Thai government faces a dilemma between maintaining high interest rate and bearing with the worsening financial crisis; and lowering interest rate but let go the value of baht. According to Bunyamanee and Nivatupumin (1998) in the *Bangkok Post Year-End 1997* Report, facing this situation, investors in the international hedge funds (that is, the spot, forward and options markets) bet with the value of US$ 10 billion on Thailand's devaluation in May. The Bank of Thailand made effort to spend US$ 4 billion to defend baht and announced that baht will not be devalued and imposed selective capital controls measures to prevent offshore speculators' access to the currency.

In six-month time from January 1997 to the end of June, Thailand's foreign reserve had reduced by US$ 6.8 billion from the level US$ 39.2 billion in January to US$ 32.4 billion in June. Eventually, on 2 July, Thailand had to float the baht, which fell by 20 percent against dollars. Further in August, the Bank of Thailand obligated US$ 23.4 billion to swap dollars for baht in the forward market. The then Prime Minster Chavalit Yongchaiyudh tried to restore foreign and domestic confidence by promising that no additional financial firms would be shut down. However, records showed that between March to August 1997, the government shut down 48 more finance firms which comprises 64% of the finance market. That was the second breaking of the promise made by the government.

Being turned down by Japan, Thailand accepted the US$ 17.2 billion from the IMF and World Bank to whom Thailand must be obliged, at their discretion, to strict conditions and agreements on restructuring its financial sector. In October, to comply with the IMF conditions, the government imposed a one baht per litre tax on oil products and foreign ownership restrictions were waived for 10 years. Three days later, due to the fierce public pressure, however, Prime Minister Chavalit had to remove the oil tax. In the *Bangkok Post* news headline "Banking sector's new look," (15 August 1998), the authority announced the taking over of Bangkok Bank of Commerce and First Bangkok City Bank by Krung Thai Bank, the largest bank with assets exceeding 1.2 trillion baht. Moreover, Laem Thong Bank merged with Ratanasin Bank; Krung Thai Thanakit Finance and Securities took over Union Bank's license and absorbed five finance companies.

At this time, the credibility of the government was at its lowest plateau as there has never been satisfactory transparency, first in the shutting down of more finance companies, then on the devaluation of baht and later the IMF restructuring package. Shortly, the finance minister resigned and baht dropped sharply past 40 baht per dollar. Finally, on 3 November, Prime Minister Chavalit resigned and Prime Minister Chuan Leekpai (who was the former prime minister from September 1992 to May 1995) took office. Baht rebounded to 37 baht per dollar.

Referring to Hicken's (1998) effects, the politicians who got elected at the time were yet to be able to work out the process of cronyism because the economic bubble burst before the expected due time. Democracy works its way as President Kim Young Sam and Prime Minister Chavalit Yongchaiyudh were out of office, allowing new reformist government under Kim Dae Jung and Chuan Leekpai to take over. In Thailand, there was also a revision of the constitution. Thus, to some extent, it reveals that the democratic system may have compounded crisis in Korea and Thailand, but it has also built in the corrective mechanisms, despite the low degree of transparency in Chavalit's government. As earlier in this article, the author rather feels more comfortable with the term *part* liberalisation.

What has become of the non-democratic governments in the region like Indonesia under President Suharto? Despite the experience that authoritarian governments like

Singapore and Hong Kong were able to overcome credible commitment problems and promote long-term growth, countries like Indonesia faced difficulty in the check-and-balance mechanism of the executive authorities. Indonesia's initial directive response to crisis seemed more decisive than that of Thailand because of the unchecked and unchallenged concentration of the presidential authority. However, the system is running high risk that the president could introduce unwelcome policy measures and, therefore, reversing the prior policy commitments. In such system, the citizens cannot oust the government, unlike in the case of Thailand. Later on in the last three months of 1997, Indonesian people were doubtful of the government's true intention on top of the rising question of succession. Since a corrective mechanism in such ruling structure never existed, citizens do not have the legal and righteous means (for example, election or re-election) to cast their option. Hence, it was very unlikely that violence can be overlooked as one of the ways to work out by the people. This had been observed clearly in the riots in the country during the years of economic crisis.

Through the election corrective mechanism, Prime Minister Chuan Leekpai was elected into the government. Though being criticised for being too risk adverse and lagging behind, Chuan's government intended to act firmly to correct Thailand's problems. On 8 December 1997, the government announced that only two of the 58 suspended securities companies would be allowed to open. Further restrictions were additionally imposed to seize Thailand's 15 domestic banks that were forced to write down capital.

7. Conclusions and a Recapitulation: Seeking Rationality out of the Loop

Tracing back to see the impressive economic performance in the miracle countries as well as Thailand, it is questionable *why* the financial institutions did take the unwise risks, when this risks were rather quantifiable given the mechanism of the market and the rationality of the market investors. One of the explanations may attribute to the political aspects of public and corporate governance. This is equivalent to referring to the composition and chemistry of the politics which make up the vertebrae axis of the making of policy design. Despite the importance of close business-government relations in the Asian miracle, it is clear and evidenced in the crisis that both the misguided government intervention as well as the part-liberalisation have the tendency to breed moral hazard, rent-seeking, cronyism and corruption. It is, thus, the role of vigilant political theorists to carefully delineate the situation in a way more comprehensible to the public.

One of the comments in World Bank (1997), Chapter 6, raises the question of how to remove discretion and manipulation of bureaucratic incentives. Then, the suggestion follows that there must be sufficient public service pay (acting as "carrots") and effective monitoring and punishing of corrupt behaviour (acting as "sticks"). However, apparent in the case of interventionist as well as liberalised states, it is the politicians not the bureaucrats who hold the discrete power. Hence, the focus should rather be placed on the first group.

From the rationale in the previous paragraphs that regulatory failures must have political roots, to emphasise: the *composition* and *chemistry* of the politics, one possible way to avoid more consequences of failure is to relocate that discrete power. Consider the case of a politician legislator. The legislator not only has collective social interests but also some electoral concerns. Thus, there is a very high tendency to perform "log-rolling". According to Babara Geddes (1994), if everybody does this, then the outcome would be what is called "politician's dilemma", where only a sub-optimal state of welfare can be achieved[3]. Once in office, the elected politicians will take into effect the composition and chemistry of the politics as discussed earlier in this article. In the most severe case, this not only led to policy failure but eventually confessed political and institutional failure when the bubble economy finally burst into the famous Thailand-originated financial crisis.

Hence, it may be recapitulated from the many works produced by Thai academics, such as Kaosa-ard (1998) and Nikomborirak (1998) and Thanapornpun (2003) that most

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[3] Nevertheless, this does not mean to imply that without the influence of the log-rolling activities, though with perfect information, the political outcome would be optimal. One must still bear in mind the inevitable possibilities that had originally explained by Marquis de Condorcet (known as the Condorcet's Paradox) and later expanded by Kenneth Arrow to include multiple voters and policies up to infinity.

policies discretely made by the authority had no solid support by careful studies by knowledgeable persons; and that a higher degree of transparency and an appropriate regulatory body are called for. One of the suggestions to "split" this discrete authority so as to increase the degree of accountability and transparency would be delegation (Kiewiet and McCubbins, 1991). By means of delegation, discrete authority can be passed to executives or bureaucratic agencies who are neutral, knowledgeable, socially-concerned and are capable of solving collective problems. Thailand, for example, delegated the task of scrutinising the health of finance companies to an independent restructuring agency. As a result, the agency was able to quickly arrive at the decision that finance companies should be liquidated. In economic sense, delegation could be considered as a "division of labour" to increase efficiency.

Moreover, in order to activate the true liberalised market, World Bank (1997) suggests that budgets, revenue collection data, statutes and rules and proceedings of legislative bodies must be regularly published. This is because any obtained funds outside the budget available to chief executives are an "invitation to corruption". Moreover, a non-government body should act as a vigorous media to cross-check on government by exposing and threatening to expose corruption, if any. Campos and Root (1996) further suggest that institutionalising business-government contacts into formal corporatist bodies can have this effect, by providing incentives for mutual checks amongst business interests. This could avoid the highly individualised dominating client relations that could lead to corruption.

The Asian financial crisis led to various social consequences such as declining income, rising poverty, education, health, crime and social violence. The post-crisis policy dimension, therefore, calls for a more focus on the issues of social security. In the past, prior to the crisis, most governments in Asia have not been sufficiently involved in these issues. An exception to this is South Korea where the social security system has been highly developed since its transition to democratic rule in the late 1980's. More consideration on the social security system is crucial to the success of the adjustment process to recovery. This is because if the public disapproves of the current state of social welfare during the recovery, then that may lead to violence or riots which retards or disrupts the adjustment process. Rodrik (1998) neatly describes the situation as "the provision of social insurance,...cushions the blow of liberalisation..., helps maintain the legitimacy of those reforms, and...averts backlashes against the distributional and social consequences of integration into the world economy."

In some societies, however, cultural or historical limitations may be significantly influential that they act as obstacles to the complete transition to the desired system of government and social security in a very short time. Hence, there are groups of academics such as Putnam (1993), Fukuyama (1995), Tendler (1997), Abeysekera et al (2000) and Tasarika (2002) who offer an alternative idea to economic recovery and sustainability, through the society's self-improvement in social welfare, which relates to the concept of "social capital". Based on the World Bank's definition, social capital comprises a combination of norms, relationships, institutions and networks influencing the quality and quantity of a society's social interactions that lead to collective actions. Particularly in Thailand, the concept of self-sufficient economy, designed by His Majesty the King's theory on integrated agriculture had been introduced earlier in 1994 and re-expressed on 4th December 1997 a few months after the renown crisis.

Furthermore, there is a literature such as Tobisson and Rudvist (1992) relating to the advantages of beneficiary involvement which leads to a more favourable development performance. For Thailand, the "compassionate" project schemes that the current government has been undergoing may be, to certain extent, considered the policy in the desired direction of the policy design in terms of the needs to increase provision of social securities. However, to perceive as such, one must strictly assume that the leaders are far-sighted enough in Olson's (1993) context[4]. Moreover, such policies must receive a careful weighing between the short-term populists' temptations versus the long-term costs and accrued debts and burdens that must be postponed to the future generation.

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[4] But, then, one can still argue that even if the leader is "far-sighted" enough, it cannot be assured that his/her decision would be best for the short-run. Moreover, there is the question of how long should this short-run period be and how much longer some portions of the society must have to sacrifice for the overall sake of the society.

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