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Injoo Sohn

In this article, I show an important connection between global financial governance and Asian regional financial governance. My findings suggest that unless the G7-dominated global financial institutions resolve the legitimacy problems, which involve inclusiveness, rule-governance, and fair returns, Asian developing countries are unlikely to place whole stock in global solutions created to deal with global (and regional) financial issues. The perceived deficiency of political legitimacy, even in the post–Asian crisis global financial architecture, drives Asian countries to become *rule makers* rather than *rule takers* through the new regional financial arrangements, such as the Bilateral Swap Arrangement under the Chiang Mai Initiative and the Asian Bond Fund. **Keywords:** legitimacy, globalization, Asian regionalism, international finance, multilateralism.

Following the Asian financial crisis of 1997–1998, a set of new financial arrangements emerged at both the global and regional levels in order to prevent future financial crises. The Financial Stability Forum (FSF), the Group of 20 (G-20), the Bilateral Swap Arrangement (BSA) under the Chiang Mai Initiative, and the Asian Bond Fund (ABF) are among the new arrangements. It may be too early to evaluate systematically the explicit impact of the new financial forums on global and regional financial governance. Yet an understanding of the motivations behind these new financial arrangements may help us to explain and predict the future trajectory of global and regional financial governance. In this article, my primary purpose is to explain the driving forces behind the growing Asian regional financial cooperation.[1] Despite the new *global* financial arrangements, why have many Asian countries become more active supporters of *regional* financial cooperation as evidenced in the creation of the BSA and the ABF?[2]

In the article, my aim is *not* to assess either the causes of the recent Asian financial crisis or the economic performance of the new Asian financial arrangements.[3] Nor is my intention to make generic arguments

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about what principles and ideologies should guide the global and regional financial arrangements. These very important issues warrant a separate article. Instead, I focus on the formal decisionmaking structures and articulated policy agendas of global and regional financial arrangements in order to examine the significant sources of the growing Asian regional financial cooperation. In doing so, I show an important connection between global financial governance and Asian regional financial governance. The underlying argument here is that Asian countries may continue to attempt to strengthen the regional financial cooperative mechanisms until the political aspects of global financial governance—namely, the problem of legitimacy—are worked out. *Legitimacy* here is used to denote political legitimacy associated with wider participation (inclusiveness), agreed systems of rules (rule-governance), and a fair sharing of adjustment costs and benefits (fair returns).

The implications of the rise of Asian financial cooperation are significant, not merely for our analysis of Asia but also for our understanding of the current and future phase of the global economy. The emergence of new regional monetary cooperative arrangements is an important step forward for an Asian regional integration project.[4] The Bilateral Swap Arrangement under the Chiang Mai Initiative and the Asian Bond Fund offer significant instruments to prevent and manage financial crises in the region and also produce a functional base for further integration. The development of the Asian regional monetary system would also complement and constrain the United States-led global financial governance by boosting the political power and autonomy of Asia vis-à-vis the rest of the world, and the United States in particular.

Broadly, this analysis suggests that technical and economic counterarguments against the effectiveness of the Asian regional arrangements alone cannot discourage Asian countries from pursuing regional multilateral solutions to future international financial problems. The perceived deficiency of political legitimacy, even in the post–Asian crisis global financial architecture, drives Asian countries to become *rule makers* rather than *rule takers* through the new regional financial arrangements. In this respect, this article investigates the independent causal effects of legitimacy on strategic choice made by states in the region.

In the next section, I discuss the conceptual framework for the problem of legitimacy with respect to global financial governance. Then I provide a brief description of changing perceptions in Asia and among the Group of Seven (G7) leaders about global financial governance after the Asian financial crisis. This is followed by an analysis of the emergence and limitations of the Financial Stability Forum and the G-20. In the last section before the conclusion, I examine the rise of the Bilateral

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Swap Arrangement under the Chiang Mai Initiative and the Asian Bond Fund.

Legitimacy and Global Financial Governance

In international relations, legitimacy usually refers to the sense of obligation to uphold international laws and contracts and to keep commitments.[5] By legitimacy, I mean that members of a relevant group not only tolerate the status quo in the personnel and structure of policy and authority, but also believe that there is little "out there" in terms of alternative institutional arrangements. In this article, the conceptualization of legitimacy moves beyond contractual obligation, which is the primary concern of the rational choice approach to politics. In the rational choice framework, obligation is created when parties enter into agreements. Obligation is thus a product of choice made by utility-maximizing actors. However, more culturally and sociologically attuned legal and international relations scholars emphasize that contractual obligations alone are insufficient to determine behavior.[6] In their view, legitimacy generates obligation and thereby links obligation to behavior. Legitimacy emerges when rules are widely applicable, provide clarity, are coherent with other rules, are relatively constant over time, and are possible to perform.[7] Without such internal legal values, legitimacy and corresponding behavioral change are less likely to emerge. Here, legitimacy is "sticky" enough that members of a group will continue to comply with rules even when the material benefits supplied by the status quo decline.

Attention to internal legal values is useful to identify how legitimacy operates among states. However, its abstract focus on legal rationality tends to be too broad to capture variations of how legitimacy is created in particular issue areas. In order to analyze the role of legitimacy in the creation of the new global and regional financial arrangements, I identify three more specific sources of political legitimacy, which are observable in the formal decisionmaking mechanisms and the explicit policy agenda of the international monetary arrangements. They are inclusiveness, rule-governance, and fair return. I do not claim that among the sources of legitimacy these three features are more important than others. Instead, I stress that they are useful conceptual tools that can explain particular global economic issues such as the emergence of Asian regional financial arrangements.

Inclusiveness refers here to wider and more meaningful participation of the members of a relevant group in the decisionmaking process

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of the global financial system. Legitimacy relies on agents in the system knowing why rules are necessary.[8] By participating in the construction of rules, the agents better understand the need for them. Legitimacy also depends on the ability of actors to gain a genuine stake in the enterprise and to feel that they have influence in the decisionmaking process. Unless state actors feel a sense of ownership in the decisionmaking structure of the global financial system, their sense of compliance decreases when material benefits decline or coercion is no longer credible.

Rule-governance refers to policymaking and implementation through a transparent, specific, and agreed-upon rule or process that has been agreed on to interpret such a rule. The absence of an agreed system of rules may increase the uncertainty and ambiguity surrounding governance and thereby expand a perceived room for dominant actors' maneuvering and arbitrary behavior in their favor. Legitimacy can be threatened, then, not only from defection by members of a group, but also by contradictions and inadequacies in the systems of rules.

The third element of legitimacy concerns the equitable sharing of costs and benefits in cooperative efforts—*fair return*. The theoretical proposition is that unless actors can expect an adequate balance between contributions and rewards, they will not participate or comply.[9] State actors tend to maintain a balance between their contributions to the international cooperative effort and the benefits they receive from it. The notion of fair return is different from the neorealist concept of relative gains.[10] The fair return hypothesis disagrees with the idea that states always base their interaction on the calculations of relative gains or losses vis-à-vis others. Rather, states seek a fair distribution of the costs and benefits of cooperative arrangements. If states are confident about the more equal sharing of the costs and benefits, they are more likely to have a sense of compliance with the arrangements.

The Changing Perceptions of Asia and the G7: Effectiveness and Legitimacy

The Asian financial crisis changed the perceptions of both Asian and G7 leaders about global financial governance. Both Asian developing countries and the G7 industrial countries increasingly questioned the effectiveness and legitimacy of the existing global financial arrangements in the aftermath of the Asian financial crisis.

First, Asian countries that experienced the conditionality of the International Monetary Fund (IMF) doubted the effectiveness of the IMF-driven global solutions. When the IMF negotiated its program with

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Thailand, Indonesia, and South Korea, it required the recipient governments to increase their interest rates and to adopt fiscal austerity. This solution resulted from the previous experience of the IMF in Latin America. In Asia, however, the IMF ignored the danger of fiscal restriction where budgets had for years been fairly well balanced. This IMF prescription depressed economic growth and raised unemployment in those IMF-assisted Asian countries. Malaysia and Hong Kong even challenged the IMF by adopting unorthodox approaches, which garnered support from China, Japan, and Russia.[11] Apart from the specific contents of the IMF solution, many Asian countries also became skeptical about the presence of IMF conditionality per se. The critics of the IMF claimed that the expansion of loan conditions resulted in a loss of precious time, whether during negotiation or implementation. The stringent program conditions make it difficult to convince a country to work with the IMF until it is absolutely necessary—almost too late for a minor cure to be effective.[12]

More importantly, the crisis-stricken Asian countries raised questions about the legitimacy of the policies imposed by the G7-centered IMF. Asian countries were, in the eyes of many Asians, subject to IMF rules without a meaningful level of representation and participation in the decisionmaking process of global financial governance.[13] Overt criticism of the IMF was muted in some quarters because the crisis-hit countries were still receiving IMF assistance; metaphorically speaking, they were understandably reluctant to criticize their doctor while undergoing treatment. By 1998, both South Korea and Thailand had new administrations that happened to be more sympathetic to the Washington Consensus on financial reform. Both governments blamed the crisis on the outgoing administrations and used the IMF to take the political blame for unpopular structural reforms. Although official governments publicly supported the IMF, their populations harbored strong resentment toward the IMF and the Washington Consensus. There was, and still is, a strong sense that the West in general, and the United States in particular, used the Asian financial crisis to advance a particular economic agenda that served selfish interests.[14] The chairman of the Thai Star conglomerate referred to IMF letters of intent as "letters of surrender." South Koreans resented the IMF because they felt that the United States had taken advantage of the Korean crisis to open the Korean economy and to buy up its precious industrial base. In late 1998, despite the public support of the Korean government for the IMF, South Korean prime minister Kim Jong Pil broke ranks to endorse the "Asian development model" and called for an independent Asian Monetary Fund.[15] Furthermore, the painful experiences of postcrisis reforms encouraged

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many Asian emerging market economies—that is, the former periphery—to demand a more equitable sharing of the adjustment costs vis-à-vis the center—that is, the United States or its G7 partners. The crisis-hit countries were discontent with the perceived unequal sharing of the adjustment costs with private international lenders headquartered in the United States and in other G7 countries.[16]

The Asian financial crisis also influenced the perceptions of the G7 regarding global financial arrangements. G7-centered decisionmaking characterized the pre-1998 international financial architecture. Prior to the Asian financial crisis, G7 members and the IMF made most of the decisions on global financial governance, with the Bank for International Settlements (BIS), the Organization for Economic Cooperation and Development (OECD), and the World Bank playing supporting roles.[17] Within this relatively exclusive circle of decisionmakers, the United States continued to enjoy "extraordinary power."[18]

The Asian financial crisis began to alter this situation by taking the formal mechanisms of international financial decisionmaking in a more inclusive direction (discussed in the next section). As Randall D. Germain notes, the G7 began to include significant developing countries in the decisionmaking mechanisms of the global financial governance for two basic reasons: effectiveness and legitimacy.[19] First, the Asian financial crisis led the G7 economies to realize a growing "mutual vulnerability." The chain of events that stretched from Thailand, to Russia, to Brazil affected the G7 economies considerably; worldwide capital and stock markets suffered significant declines during an Asian-induced recession. In order to govern global finance effectively, the G7 realized that it could no longer exclude key emerging economies from their governance. Second, in order for emerging market economies to reform their financial policy and practice, they needed to have a meaningful level of input into the reform efforts of global financial governance. Political legitimacy is the core of these concerns. Without due representation and participation, developing countries have every reason to challenge the legitimacy of the policies imposed by the G7-dominated international financial institutions.

The New Global Financial Arrangements and Their Limitations

These changing perceptions contributed to the emergence of the Financial Stability Forum and the G-20.[20] In 1999, Hans Tietmeyer (former head of Deutsche Bundesbank) suggested the creation of the FSF. Tietmeyer

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noted in his report that effective financial regulation relied on an adequate flow of information and proposed a forum whereby central bankers, finance ministry officials, and financial regulators could meet to discuss global financial issues. From its third meeting in Singapore (March 2000), the FSF extended its membership to include Australia, Hong Kong, the Netherlands, and Singapore.[21] A G7 communiqué noted that "while the [Financial Stability] Forum will initially be the initiative of the G7 countries, we envisage that over time additional national authorities would be included in the process. The issues to be addressed affect all countries, including both industrial and emerging market economies, and the G7 regards this initiative as a step toward broader participation."[22]

In contrast to the highly selective FSF (that is, only four non-G7 national representatives), the G-20 includes countries from throughout the world. The G-20 brought together finance ministers and central bank governors from Argentina, Australia, Brazil, China, India, Indonesia, Mexico, Russia, Saudi Arabia, South Africa, South Korea, and Turkey, along with their G7 counterparts and a senior representative from each European Union (EU) member, the IMF, and the World Bank. G7 finance ministers decided to establish the G-20 in September 1999 when they committed to ensure broader participation in discussions of international financial affairs among countries whose size or strategic importance gave them a particularly crucial role in the global economy.

Although the reforms initiated by the G7 to date might represent small steps in the right direction toward enhancing political legitimacy, they have not yet met the expectations of emerging market economies. In the eyes of many developing countries, the FSF featured heavy G7 representation. Although the G7 regarded this initiative as a step toward broader participation, their sense of "broader participation" clearly implied the inclusion of the few countries that are most actively involved in global financial markets. The new FSF excluded key emerging economies such as China, India, Indonesia, South Korea, Malaysia, and Thailand. Even the four new members were not given the same depth of representation enjoyed by the G7: the Netherlands, Australia, Hong Kong, and Singapore had a single representative rather than the three allocated to their G7 counterparts. The G7 attempted to address this deficiency by allowing non-G7 countries to participate in the FSF working groups. For example, Thailand, India, and Mexico were included in the working groups on the Implementation of Standards. But the participation of the non-G7 countries was at the discretion of the FSF members and therefore not a sustainable form of representation.

It is conceivable that the more inclusive G-20 was created, in part, to complement the more selective FSF and thereby to deflect criticism

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that participation in the latter needs to be broadened to include some developing countries.[23] In creating the G-20, the G7 clearly attempted to enhance the legitimacy of the G7-dominated decisionmaking process of international financial matters.[24] Although the G7 promoted the G-20 as a mechanism to include non-G7 countries, it also set limits on its political influence within the existing global financial governance structure. For instance, after its first meeting, German and Canadian finance ministers noted that the G-20 did not want to be a decisionmaking body.[25] Given that the G-20 continued to be a nondecisionmaking body, the involvement of non-G7 countries would make little difference in the actual decisionmaking process of global financial governance. In addition, unlike the G7, there are no provisions for a G-20 summit. This suggests a secondary and limited role of the G-20 compared to the G7.

Furthermore, the governing rules of the G-20 and the FSF remained minimal. The rules guiding membership selection and agenda selection remained vague. For instance, there were no explicit standards to explain why Indonesia rather than Malaysia was included, or Turkey rather than Thailand, in the G-20. Likewise, it is not clear whether or how the non-FSF members would continue to participate in future FSF working groups. Without a globally agreed system of rules, the FSF and G-20 remained vulnerable to charges that they were puppet institutions created by the G7.[26]

In addition to the elements of inclusiveness and rule-governance, the FSF and the G-20 also remained vulnerable to the charge that they would entail the *unfair* sharing of adjustment costs and benefits. States are unlikely to agree to collaborate unless they have some confidence in the equal sharing of the costs and benefits associated with their cooperative efforts. In the case of global financial governance, the burdens of the financial reforms were asymmetric. They were heavily weighted by policy changes required of borrowers and debtors, whereas much less burden was put on lenders and creditors. The reforms focused on remedying financial fragility in countries at the periphery of the global financial system, rather than reforming the system as a whole or, for that matter, even calling attention to the shortcomings in countries at the center. Addressing *domestic* vulnerability to financial crises appears to be the prevailing focus of the G-20. For example, the priority areas of the G-20 during its fifth meeting in 2003—sound domestic financial markets, increased financial liberalization, effective regulatory policies and supervision, and the Action Plan on terrorist financing—are important but not as wide ranging as one might expect given the concerns of developing countries about the structural danger of international capital mobility. The major outcome of this meeting did not reduce the suspicion

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that the G-20 was a mechanism to support existing policies favored by the G7. In contrast, the scope of the three FSF working groups, which was broader than the initial focus of the G-20, was to examine some of the vital *international* aspects of the recent financial turmoil: hedge funds, transnational capital flows, and offshore financial centers. However, as Roy Culpeper notes, the FSF resisted recommending any radical policy changes in these areas.[27] Hedge funds, for example, were widely suspected of complicity in the speculative frenzy around the Asian crisis. The FSF working group considered, but did not recommend, direct regulation of currently unregulated hedge funds, although it kept the door open to such a possibility. Similarly, although the FSF focused on urging emerging markets to develop sound guidelines for sovereign debt and liquidity management, it was rather critical about managing or controlling capital flows themselves. In other words, the FSF and the G-20 focused primarily on the domestic aspect of the reforms (in developing countries in particular), as opposed to the international aspect of the reforms, which might involve painful adjustment for the G7 as well as non-G7 countries.

New Asian Regional Financial Arrangements

The perceived deficiency of political legitimacy, even in the new global financial arrangement, facilitated the Asian pursuit of regionally differentiated solutions over global ones. The Asian skeptics of the G-20 and the FSF claim that these new global financial arrangements have little or no impact on the power configuration within the G7-centered decision-making structure of global financial governance.[28] In other words, these new global financial arrangements reflect a cosmetic change rather than a substantive change in global financial governance.

In this context, for example, Chinese prime minister Zhu Rongji declared in November 2000 that China stood "ready to work with other East Asian countries for the reform of the current international financial architecture" and was open to "all ideas" about financial cooperation in the region.[29] Eisuke Sakakibara, former Japanese vice-minister of finance, also spoke out for a regional monetary regime in East Asia. In August 2003, he said that it was timely for East Asian countries to express their view to the world and to convince the United States that an East Asian community had to be created.[30] Likewise, Il Sakong, chairman of the Korean Institute for Global Economics, argued that Asia needed some kind of economic defensive mechanism at the regional level because it could not be expected at the global level.[31] Malaysian prime minister

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Mahathir Mohamad has been consistent in his provocative call for a regional monetary fund independent of the IMF. According to Mahathir Mohamad, "We [East Asian countries] have to have an Asian Monetary Fund simply because the IMF is not as independent as it should be. As we know, there are other hands which are controlling it and those hands have other ideas contrary to the prosperity of East Asia."[32] Chalongphob Sussangkarn, president of the Thai Development Research Institute, also said that "after the crisis, countries in the region had very little input in designing the prescribed medicines (mainly from the IMF). . . . With vast financial resources in the region, East Asia needs to have more say in how the global financial system should be reformed."[33]

It should be also noted that Thailand and Malaysia have been the most enthusiastic and vocal actors among Asian countries in their willingness to propose and sell the idea of new regional financial arrangements. Thailand and Malaysia served as host countries in the creation of the Chiang Mai Initiative (an Asian regional financial swap arrangement) and the first East Asia Congress (an international conference regarding the concept of an East Asian community), respectively. It is conceivable that the high visibility of the two countries correlates to the fact that, unlike South Korea and Indonesia, for example, Thailand and Malaysia were excluded from both the G-20 and the FSF. Their sense of being excluded from the new global financial architecture might enhance their behavioral propensity toward regional financial arrangements.

Against this backdrop, Asian countries have sought to develop new regional financial arrangements. Two initiatives in particular have been important in Asia's efforts to promote regional monetary cooperation: the Bilateral Swap Arrangements under the Chiang Mai Initiative, and the Asian Bond Fund. These two regional financial arrangements intend to supplement existing global financial governance in general, and also reduce the need for IMF support, in particular, in crisis management and finance for development. Strong regional reserve funds would partially deter would-be speculators from attacking the currencies of individual countries in the region and thereby prevent or at least minimize the destabilization of regional trade and financial relations. The development of regional bond markets would also mobilize the region's vast pool of savings for long-term investment in Asia rather than in Europe or the United States.

The finance ministers of the Association of Southeast Asian Nations (ASEAN) Plus Three decided at their meeting in Chiang Mai, Thailand, in May 2000, to establish the first regional financing arrangement in East Asia under the so-called Chiang Mai Initiative, which would comprise an expanded ASEAN Swap Arrangement (ASA) and a network of

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bilateral swap arrangements (BSAs) among ASEAN countries, China, Japan, and South Korea. Since then, the ASA has been enlarged to U.S. $1 billion in size (effective November 2000), and a number of BSAs have been signed. As of April 2004, sixteen BSAs have been successfully concluded, with a combined total size of $36.5 billion.[34] For example, Japan has concluded its negotiations with Thailand ($3 billion), the Philippines ($3 billion), Malaysia ($1 billion), South Korea ($2 billion), and Indonesia ($3 billion); South Korea has concluded its negotiations with China ($2 billion), Thailand ($1 billion), Malaysia ($1 billion), and the Philippines ($1 billion); and China agreed with Thailand ($2 billion), Indonesia ($1 billion), and Malaysia ($1.5 billion) on BSAs along with its arrangements with Japan and South Korea.

These BSAs are designed to provide liquidity support for the member countries that experience short-run balance-of-payment deficits in order to prevent an extreme crisis or systemic failure in a country and a subsequent regional contagion as occurred in the recent East Asian financial crisis. The BSA agreements allow an immediate disbursement of up to 10 percent of the maximum amount of drawing, when swap-providing countries agree. Although the BSA has proven a significant postcrisis initiative to come out of Asia, it has certain limitations. First, the size of the BSA (which now amounts to $36.5 billion) is relatively small compared to the emergency assistance required by the crisis-hit countries at the time of the 1997 crisis (Thailand alone requested $17.2 billion) and the foreign exchange reserves held by the ASEAN Plus Three countries (which now amounts to $1.5 trillion). A recent study by the Asian Development Bank (ADB) therefore recommends that ASEAN Plus Three countries consider expanding and multilateralizing their swap lines initially by earmarking a certain amount of their foreign exchange reserves for short-term emergency financing. In the medium term, according to the ADB study, ASEAN Plus Three could also consider establishing a central reserve fund where the earmarked reserves could be merged and managed in line with strengthened regional economic monitoring.

Furthermore, the BSA is also limited in its independent use of the swap lines. Countries drawing more than 10 percent from the facility are required to accept an IMF conditionality. In this sense, the current BSA is complementary to the financial assistance of the IMF at the moment. Some participating countries have opposed the linkage of the BSA with an IMF conditionality. For instance, Malaysia advocates complete independence of the BSA (under the Chiang Mai Initiative) from the IMF. By contrast, other members, in particular Japan and China, have argued for the importance of forging a cooperative relationship

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with the IMF at an early stage of the BSA development to make it more credible. They have persuaded Malaysia and other opposing members to accept the linkage of the BSAs with an IMF conditionality as a temporary arrangement until a formal surveillance mechanism is put in place. Malaysia agreed to the IMF linkage on the condition of establishing a study group to examine the types of monitoring and surveillance systems, which is necessary for the BSA (under the Chiang Mai Initiative) as an independent regional financial arrangement. At the fifth ASEAN finance ministers' meeting in April 2001 in Kuala Lumpur, the participating countries agreed to review the issues of the IMF linkage with the BSAs in three years. In May 2005, the finance ministers of East Asian governments agreed to double the proportion of emergency funds that could be drawn without IMF conditionality from 10 percent to 20 percent. This represents the incremental approach taken by East Asian countries in loosening their adherence to IMF conditionality. Whether or not the BSAs eliminate their IMF linkage in the near future, such a regional liquidity fund intends to challenge the IMF monopoly on crisis management in the long term.

In the meantime, eleven central banks in East Asia and the Pacific announced in June 2003 that $1 billion of the Asian Bond Fund (ABF1) is to be invested in U.S. dollar-denominated regional bonds. The member countries include Australia, China, Hong Kong, Indonesia, Japan, South Korea, Malaysia, New Zealand, the Philippines, Singapore, and Thailand.[35] Among those countries, Thailand announced its contribution of $120 million to the ABF; South Korea agreed to invest more than $100 million; Japan, Singapore, and the Philippines each provided $100 million; Australia and Indonesia subscribed $50 million each; and New Zealand pledged $25 million to the ABF. At the second Asia Cooperation Dialogue (ACD) meeting, which was held in Chiang Mai, Thailand, in June 2003, eighteen ACD countries supported the Asian Bond Fund Initiative and the roadmap for Asian bond market development by adopting the Chiang Mai Declaration.[36] Additionally, India pledged to contribute another $1 billion to the Asian Bond Fund. In April 2004, the eleven member countries unveiled the initial structure of a planned second Asian Bond Fund (ABF2), which will invest in local currency-denominated Asian bonds.

The establishment of the Asian Bond Fund by Asian central banks ultimately aims to (1) bring back Asian foreign reserves (amounting to $1.5 trillion) that were traditionally saved in Europe or in the United States to be used in bond investments throughout Asia, (2) provide a catalyst, as a lead investor, for private investors to consider vast long-term investment in Asian issues, and (3) shield the region from external

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vulnerabilities by building more robust and diversified local capital markets. Many Asian policymakers believe that the Asian financial crisis would have been less severe if local bond markets had been more developed and financial intermediation in the crisis-affected countries had not been so heavily concentrated on banks.[37] With a starting capital of $1 billion, the fund initially invests in sovereign and quasi-sovereign bonds issued by Asian governments in the international markets. During the next step, the Asian Bond Fund will extend the investment into various local bond markets in local currencies. The supporters of the ABF hope that, in the medium and long run, the fund will encourage and attract other investors including private money in Asia, such as insurance companies in Japan, mutual funds in Hong Kong, or pension funds in Singapore, to participate in the market. The member countries anticipate that the investment in the bond market of the ABF will lead to greater liquidity, increased issuance, and better lending terms for governments and corporations and prevent a repeat of a possible future financial crisis. There is a growing interest among governments in the region to open their bond markets to foreign issuers. Thailand, for instance, announced in April 2004 that it would issue 30 billion baht of currency-denominated bonds through the Asian bond market. China also recently agreed, in principle, to allow international financial institutions such as the Asian Development Bank to issue renminbi-denominated bonds, and related rules and regulations of such issues are currently under consideration.[38]

One might argue that a series of potential political and economic hurdles will frustrate the Asian regional initiatives. Among the commonly cited obstacles to cooperation in Asia are economic diversity, interstate political rivalry, and the lack of domestic regulatory capacity.[39] U.S. opposition to the emergence of an Asia-for-Asia multilateral institution also may hinder the Asian initiatives as in the case of strong U.S. opposition to Japan's proposal for an Asian Monetary Fund in the late 1990s. The in-depth discussion of political and economic obstacles facing the Bilateral Swap Arrangement under the Chiang Mai Initiative and the Asian Bond Fund is beyond the scope of this article.[40] Nevertheless, it is noteworthy to briefly mention the current attitudes of the G3 (the United States, the European Union, and Japan) toward new Asian regional monetary cooperation. All three world economic powers have not yet challenged the new Asian financial arrangements. Japan, which has a dual identity as a G7 member and an Asian country, has been supportive of Asian regional financial arrangements, because many Japanese view the U.S.- and IMF-led solutions to the Asian crisis as a direct challenge to their country's economic and ideological interests in

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the regional economy.[41] For the EU and the United States, the temporary linkage of the BSA with the IMF seems to reduce their concerns about the emergence of exclusive regional arrangements in Asia. Furthermore, the recent emphasis many Asian leaders have placed on the Asian Bond–Eurobond linkage and the creation of a Euro Bond Market in Asia helped to mobilize EU support for the idea of an Asian Bond Market.[42] In line with Asian-European financial cooperation, for example, eleven central bank governors from the Executives' Meeting of East Asia–Pacific Central Banks (EMEAP), the president of the European Central Bank, and twelve governors from the Eurosystem national central banks held a joint high-level seminar in Singapore in July 2004. The purpose of the seminar was to exchange views on issues that are relevant to both Europe and the East Asia-Pacific region and to consolidate relations between EMEAP and the Eurosystem.

Conclusion

After the Asian financial crisis precipitated demands for a new global financial arrangement, there were signs that the G7 had finally begun to engage more expansively in dialogue with the rest of the world. Those aspirations have manifested themselves in the Financial Stability Forum and the G-20. But as this review of their progress to date indicates, there is little so far to suggest that the G7 have fully added the significant elements of legitimacy (inclusiveness, rule-governance, and fair returns) to the new global financial arrangements.

The long-term impact of the developing countries' inclusion in the decisionmaking mechanisms of the global financial governance is an open question: how the developing countries—the former periphery of the global financial system—will use the G-20 and the FSF. It also remains to be seen whether the United States and its G7 allies will challenge the further development of the BSA and the ABF in Asia. In particular, what the United States may do in the face of coordinated Asian collective action on regional financial arrangements remains unknown. The United States has never before been confronted with such actions.

At the moment, despite the attempt of the G7 to enhance the effectiveness and legitimacy of global financial governance, non-G7 Asian countries remain skeptical about the political legitimacy in the decisionmaking of the new postcrisis global financial arrangements, such as the FSF and the G-20. Such a lingering skepticism, which reinforced Asia's discontent with the U.S.- and IMF-led global solutions to the Asian crisis, set in motion the new Asian regional financial arrangements. My

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findings suggest that unless the G7-dominated global financial institutions resolve the legitimacy problems, which involve inclusiveness, rule-governance, and fair returns, Asian developing countries are unlikely to place whole stock in global solutions in order to deal with global (and regional) financial issues. Rather, despite potential political and economic constraints, Asian emerging market economies will continue to seek regional alternatives (or supplements) while encouraging broader participation, establishing a globally agreed-on system of rules, and sharing more equally in the adjustment costs regarding global financial governance. In this sense, one may cautiously anticipate that the new Asian regional arrangements will give Asia added voice in shaping the new global financial architecture. The regional arrangements could provide Asia with the leverage to contest an Anglo-American view of how the global economy is organized and managed.[43] ⊕

Notes

Injoo Sohn is a Ph.D. candidate and lecturer in political science at George Washington University. His research interests include international relations theory, Asian regionalism, and the politics of China and Korea. His doctoral dissertation examines China's multilateral diplomacy toward Asian financial cooperation.

1. This article distinguishes between regional cooperative mechanisms and relatively apolitical integration of regional economics (or regional interdependence). It is concerned with the regional cooperative mechanism, defined as the policy-led process of creating certain cohesive arrangements or institutions in the region.

2. "Asia" refers here to the countries of East and Southeast Asia. South Asian countries do not, therefore, form part of my analysis.

3. For the heated debates over the desirability and feasibility of the recent Asian financial cooperation, see C. Randall Henning, *East Asian Financial Cooperation* (Washington, D.C.: Institute for International Economics, 2002); Yung Chul Park, "Beyond the Chiang Mai Initiative: Rationale and Need for Decision-Making Body and Extended Regional Surveillance Under the ASEAN+3 Framework," available online at http://soback.kornet.net/~ycpark/pub/00bc.pdf (accessed 1 September 2003); and Barry Eichengreen, "What to Do with the Chiang Mai Initiative," *Asian Economic Papers* (Washington, D.C.: Center for Strategic and International Studies, winter 2003), available online at Lexis-Nexis (accessed 29 July 2003).

4. Heribert Dieter and Richard Higgott, "Explaining Alternative Theories of Economic Regionalism: From Trade to Finance in Asian Co-operation?" *Review of International Political Economy* 10, no. 3 (2003): 430–454.

5. For example, see Andreas Hasenclever, Peter Mayer, and Volker Rittberger, *Theories of International Regimes* (Cambridge: Cambridge University Press, 1997); and Thomas M. Franck, *The Power of Legitimacy Among Nations* (Oxford: Oxford University Press, 1990).

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6. For the constructivist-rationalist debate over obligation, see Martha Finnemore and Stephen J. Toope, "Alternative to 'Legalization': Richer Views of Law and Politics," *International Organization* 55, no. 3 (2001): 745–758; and Judith Goldstein, Miles Kahler, Robert O. Keohane, and Ann-Marie Slaughter, "Response to Finnemore and Toope," *International Organization* 55, no. 3 (2001): 759–760.

7. Thomas M. Franck, *The Power of Legitimacy Among Nations;* and Gerald J. Postema, "Implicit Law," *Law and Philosophy* 13 (1994): p. 361.

8. Postema, "Implicit Law," p. 361.

9. Wayne Sandholtz, *High-Tech Europe: The Politics of International Cooperation* (Berkeley: University of California Press, 1992), p. 15.

10. A clear statement of the neorealist notion of relative gains is in Joseph M. Grieco, *Cooperation Among Nations* (Ithaca: Cornell University Press, 1990).

11. See "Leading Asian Nations Ganged Up Yesterday. . . ," available online at www.euromoney.com (posted 30 September 1999).

12. Devesh Kapur, "The IMF: A Cure or a Curse?" *Foreign Policy* (summer, 1998).

13. Related to this point, a UN Task Force argued that "[IMF] conditionality should not include issues related to economic and social development strategies and institutions, which, by their very nature, should be decided by legitimate national authorities, based on broad social consensus." See United Nations, "Toward a New International Financial Architecture," Report of the Task Force of the Executive Committee on Economic and Social Affairs of the United Nations, 21 January 1999 (available online at www.attac.org/fra/orga/doc/un.htm).

14. J. C. Y., "U.S. Using Japan Bashing to Undermine 'Asian Mentality': Economic Crisis Chance to Push Market Principles," *Nikkei Weekly,* 22 June 1998.

15. Yong-bae Shin, "PM Kim Bucks Government's Stance on Creation of Asian Monetary Fund," *Korea Herald,* 1 December 1998.

16. Richard Higgott and Nicola Phillips, "Challenging Triumphalism and Convergence: The Limits of Global Liberalization in Asia and Latin America," *Review of International Studies* 26, no. 3 (2000).

17. Eric Helleiner, *States and the Reemergence of Global Finance* (Ithaca: Cornell University Press, 1994); Louis W. Pauly, *Who Elected the Bankers: Surveillance and Control in the World Economy* (Ithaca: Cornell University Press, 1997); Susan Strange, *Mad Money: When Markets Outgrow Governments* (Manchester: Manchester University Press, 1998).

18. Susan Strange, "Still an Extraordinary Power: America's Role in the Global Monetary System," in Raymond Lombra and William Witte, eds., *The Political Economy of International and Domestic Monetary Relations* (Ames: Iowa State University Press, 1982).

19. Randall D. Germain, "Global Financial Governance and the Problem of Inclusion," *Global Governance* 7, no. 4 (2001): 412–414.

20. Information on the FSF is available online at www.fsforum.org; information on the G-20 is available online at www.g20.org.

21. In addition to national participants responsible for overseeing domestic financial stability, the FSF comprises representatives of the IMF, the World Bank, the Bank for International Settlements (BIS), and the OECD; representatives of the Basle Committee on Banking Supervision, the International Organization of

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Securities Commissions, and the International Association of Insurance Supervisors; and representatives of the two BIS-based committees—the Committee on the Payment and Settlement System, and the Committee on the Global Financial System.

22. Group of Seven, "Communiqué of G-7 Finance Ministers and Central Bank Governors," 20 February 1999, available online at www.g8.utoronto.ca/finance/fm022099.html.

23. Montek S. Ahluwalia, "The IMF and the World Bank in the New Financial Architecture," in *International Monetary and Financial Issues for the 1990s: Research Papers for the Group of 24* (New York: United Nations 1999).

24. Tony Porter, "The G-7, the Financial Stability Forum, the G-20, and the Politics of International Financial Regulation," paper presented at the International Studies Association annual meeting, Los Angeles, California, 15 March 2000, available online at www.library.utoronto.ca/g7/g20/g20porter/index.html.

25. "G20 to Contribute to Prevention of Financial Crises," BBC Monitoring International Reports, 16 December 1999, available online at www.ft.com.

26. Porter, "The G-7, the Financial Stability Forum, the G-20, and the Politics of International Financial Regulation."

27. Roy Culpeper, "Systemic Reform at a Standstill," paper presented at the conference "Critical Issues in Financial Reform: Latin-American/Caribbean and Canadian Perspectives," Munk Centre for International Studies, University of Toronto, 1–2 June 2000.

28. This view has been strongly corroborated in confidential interviews with IMF staff economists from East Asia. Interviews at the IMF, Washington, D.C., 9 September 2003.

29. *Malaysian National News Agency*, 25 November 2000.

30. *New Straits Times*, 5 August 2003.

31. *Financial Times*, 6–7 May 2000.

32. *New Straits Times*, 5 August 2003.

33 For this statement, see Chalongphob Sussangkarn (president of Thailand Development Research Institute), "East Asian Financial Cooperation," paper presented at the First East Asia Congress, Kuala Lumpur, Malaysia, August 2003; available online at www.jikonlai.com/blogs/international_finance/East_Asia_Congress_August_2003/East%20Asian%20Financial%20Cooperation.Chalangphob%20Sussangkarn.ppt.

34. Asian Development Bank Regional Economic Monitoring Unit, "Chiang Mai Initiative," available online at http://aric.adb.org/pdf/CMI_currentstatus.pdf (accessed 25 May 2004).

35. Given the inclusion of Australia and New Zealand, the ABF cannot be defined as a pure "Asian" form of regional economic cooperation. However, it is also inappropriate to regard the ABF as an "Asia Pacific" one due in part to the exclusion of the United States and other non-Asian APEC members.

36. Thailand initiated an "Asia-for-Asia" network through the creation of the ACD to facilitate a broad range of cooperation among Asian countries. Whereas other regional cooperative frameworks (for example, APEC Finance Ministers' Meeting, ASEAN Plus Three, and the Executives' Meeting of East Asia Pacific Central Banks [EMEAP]) play their part in the technical support of the Asian Bond Market, the ACD provides the backbone needed to ensure that the Asian Bond Market has the firm political support of Asian leaders. "Asian Bond Market Offers Regional Stability," *The Nation* (Thailand), 30 May 2003.

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37. For example, see keynote address by Mme. Khempheng Pholsena (vice-president of Asian Development Bank), at the Euromoney conference "The Asia-Pacific Bond Congress: A New Maturity," Hong Kong, 9 July 2004, available online at www.adb.org/Documents/Speeches/2004/ms2004043.asp.

38. Ibid.

39. For the critical review of obstacles to Asian cooperation, for example, see Natasha Hamilton-Hart, "Asia's New Regionalism: Government Capacity and Cooperation in the Western Pacific," *Review of International Political Economy* 10, no. 2 (2003): 222–245.

40. For policy suggestions about recent Asian regional institutionalization in general, see, for example, Shiping Tang, "Institutional Building Under '10+3': Tackling the Practical Issues," *Global Economic Review* 31, no. 4 (2003).

41. For Japanese approaches to regional monetary cooperation, see, for example, Saori N. Katada, "Japan and Asian Monetary Regionalization," *Geopolitics* 7, no. 1 (2002); and Henry Laurence, "Japan and the New Financial Order in East Asia," in Leslie E. Armijo, ed., *Debating the Global Financial Architecture* (New York: State University of New York Press, 2002).

42. For this point, see "ASEM Forum to Boost Asian Bond Market," *The Nation* (Thailand), 22 July 2003.

43. For a similar view, see Richard Higgott and Martin Rhodes, "After the Crisis: Beyond Liberalization in the Asia Pacific?" *Pacific Review* 13, no. 1 (2000):1–19.

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