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2nd DRAFT

Towards a Coordinated Macroeconomic Expansion Among China, Japan, Korea, and other Asian economies

The recession in the United States and parts of Europe is likely to be severe and prolonged, and the Asian economies should take urgent and coordinated actions to protect their economic growth in the face of recessionary conditions in the U.S. and Europe. Such counter-cyclical policies should include monetary, fiscal, and exchange rate actions. By undertaking such policies in a coordinated manner, the Asian economies will achieve much larger and much more durable results than they would achieve through unilateral actions. The leadership in East Asia rests with the three largest economies: China, Japan, Korea, and ASEAN. Many other countries in East Asia, South Asia, and Oceania are likely to join in the counter-cyclical policies.

The likely severity of the coming U.S. downturn should be noted. U.S. households are deeply in debt after many years of negative saving. Credit conditions for these households have tightened dramatically; a drop in spending is virtually certain. Declines in housing values and equity prices will probably reach $15 trillion from the peak. Layoffs are on the rise. All of this will result in a very sharp drop in consumption spending and private investment outlays. The U.S. will therefore likely experience a dramatic downturn, with severe spillovers to other parts of the world. Those spillovers can include: falling exports from Asia to the U.S., a weaker dollar, and a withdrawal of credit lines from U.S. banks and U.S. investors in Asia.

The G-20 will meet in Washington on November 15. We recommend that the major Asian economies arrive at that meeting with a coordinated Asian macroeconomic policy framework already in hand. Macroeconomic expansion in Asia will not only help to sustain Asia’s own economic growth and employment levels, but will also help to put a floor on the coming global slowdown. Higher growth in Asia will also mean more sales of U.S. goods in Asian markets, thereby helping to moderate the U.S. and European recessions as well. For this reason, coordinated macroeconomic expansion among China, Japan, and Korea will be highly appreciated in all other parts of the world.

The following steps should be undertaken in the nearest future:

1. Announce that China, Japan, and Korea will work closely amongst themselves, and with other countries in the region, to ensure that Asian growth remains robust even during this difficult period for the U.S. and Europe.

2. Provide large swap lines between the three central banks, to augment the swap lines that the U.S. Fed has recently extended to Korea and other countries.

3. Remove any kind of IMF involvement from the operations of these swap lines.

4. Announce a joint fiscal expansion, appropriate for each country. China, for example, will focus on urban infrastructure, public housing, and tax cuts. Japan and Korea will identify their own respective high-social-return public investment projects and/or tax cuts. The Government of Japan may also purchase equities in order to put a floor under declining equity prices.

5. Announce a joint monetary expansion, such as another round of coordinated interest rate reductions.

6. Announce that all three countries will abjure from beggar-thy-neighbor exchange rate adjustments, and indeed will strive to keep their currency values relatively stable against a basket of dollars and euros. In particular, the Bank of Japan will resist excessive yen appreciation and will call upon the Fed and the ECB to support Japan in joint currency interventions if needed to keep the yen at or above 100 yen per dollar.

7. Establish a committee of senior Ministry of Finance and central bank officials of China, Japan, and Korea to set the coordinated package of counter-cyclical measures, and to monitor the ongoing crisis on a frequent, regular basis, and in-depth basis.

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