



Asia-Europe: The Third Link

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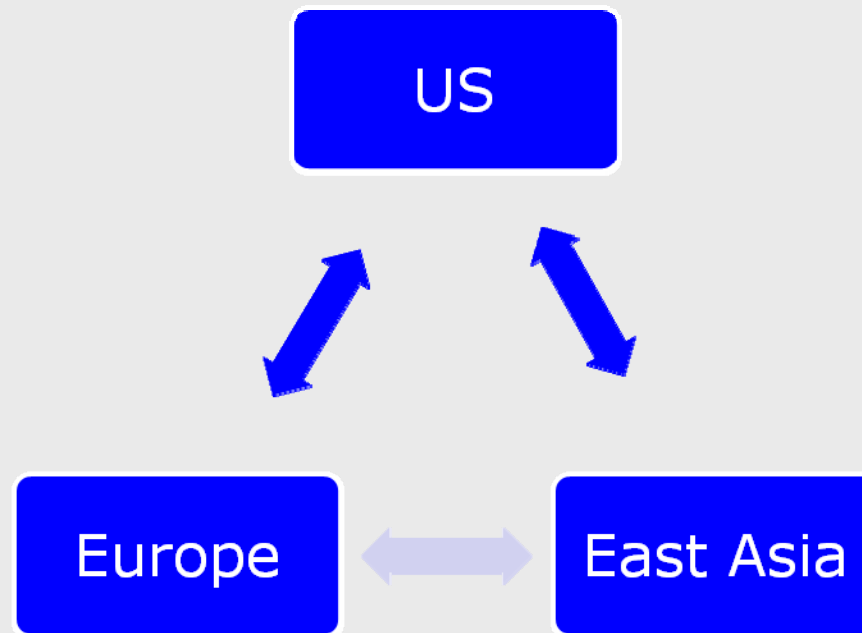
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Motivation

Prevailing view of the world economy is polarized

Is this view correct?





Outline

- 1. Map of the world**
- 2. Bilateral linkages**
- 3. Implications for shock transmission and for adjustment**
- 4. Conclusions**



1. A map of the world

- **4 regions:**
 - East Asia (ASEAN+ 3)
 - Europe (EU27 + Switzerland)
 - North America (US, Canada and Mexico), and
 - The Rest of the World

| | East Asia | | Europe | | North America | |
|---------------------------|-------------|-------------|-------------|-------------|---------------|-------------|
| | <i>1996</i> | <i>2006</i> | <i>1996</i> | <i>2006</i> | <i>1996</i> | <i>2006</i> |
| GDP (current) | 24 | 20 | 32 | 31 | 29 | 32 |
| GDP (PPP) | 22 | 24 | 26 | 24 | 27 | 26 |
| Population | 29 | 32 | 8 | 8 | 6 | 7 |
| Trade* | 23 | 23 | 25 | 23 | 20 | 19 |
| Financial assets** | n.a. | 19 | n.a. | 33 | n.a. | 37 |

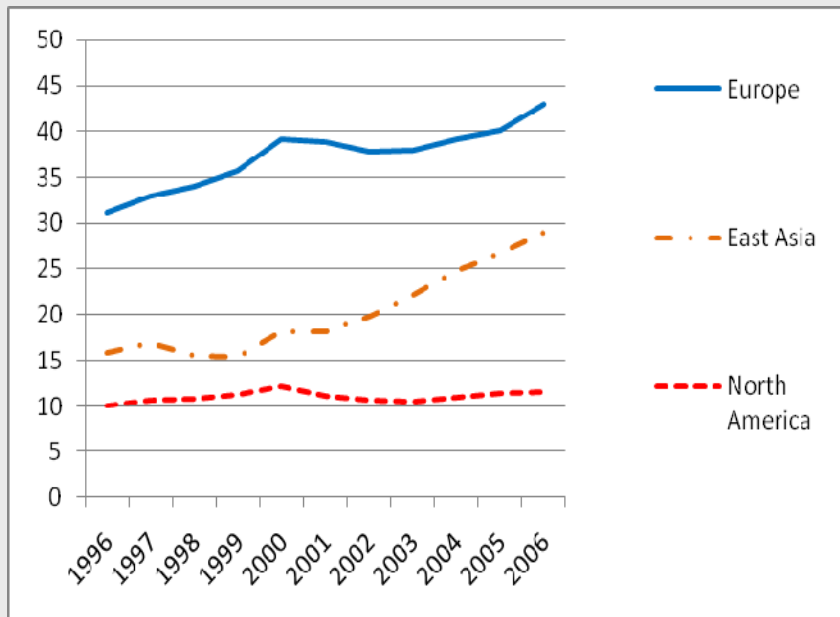


Regional integration

Uneven progress

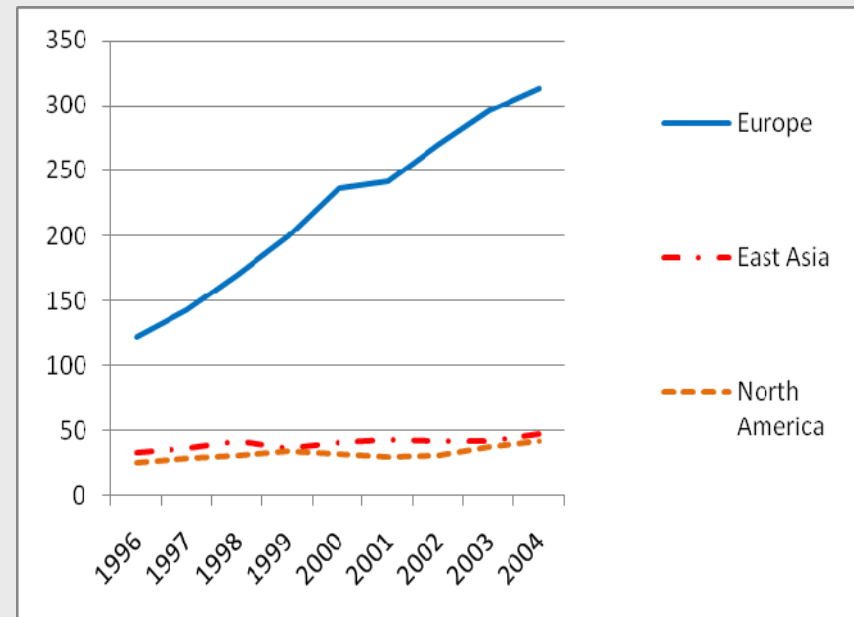
Trade

(Intraregional trade, % of GDP)



Finance

(Intraregional holdings of assets and liabilities, % of GDP)



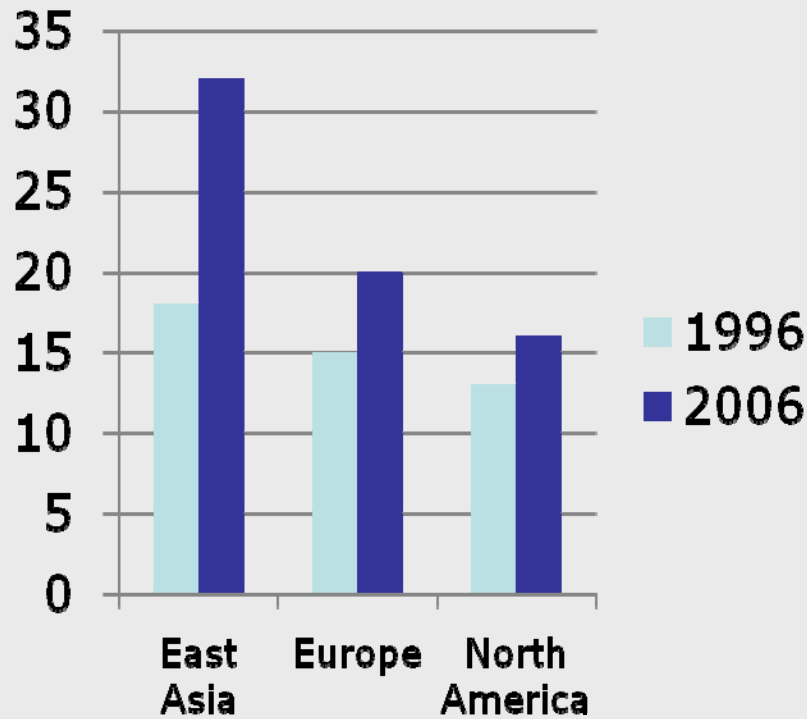


Global integration

Fast development

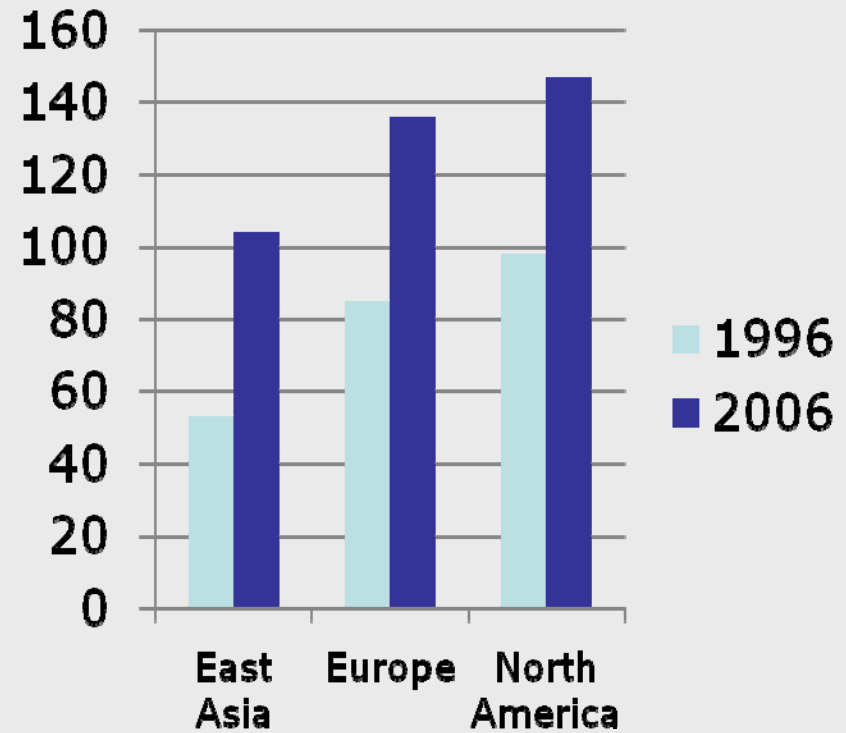
Trade

(Extraregional trade, %of GDP)



Finance

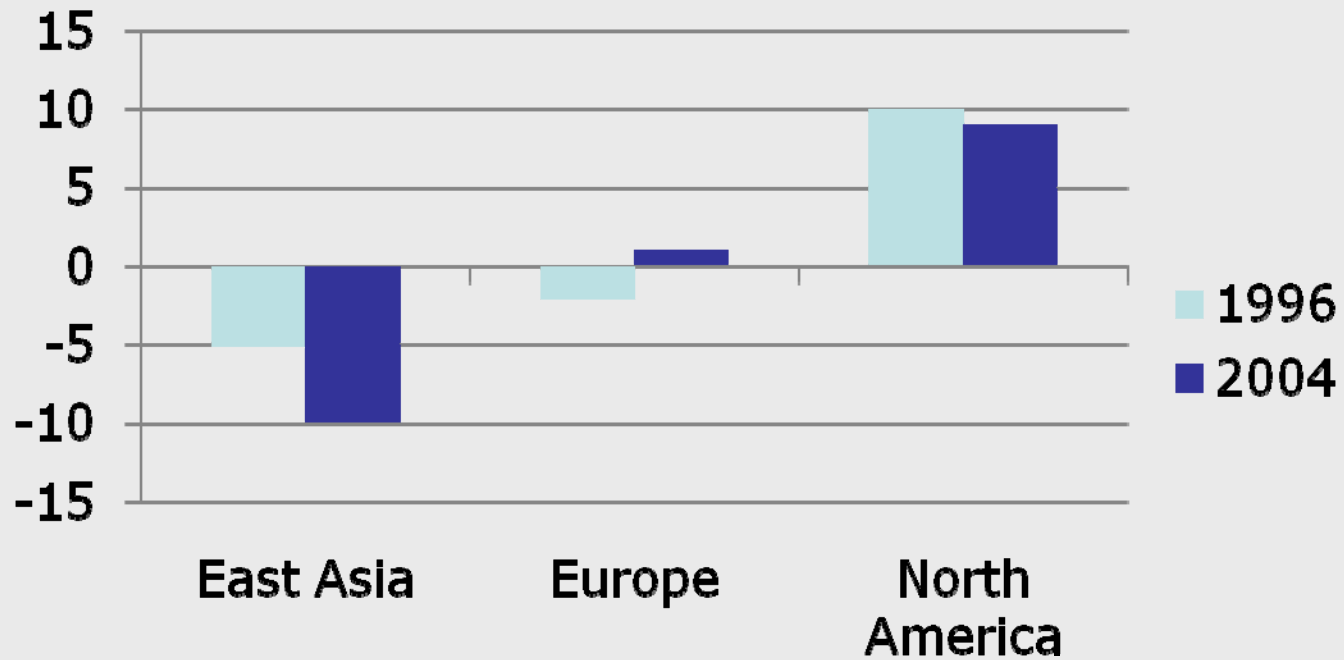
(Extraregional stocks, %of GDP)





Still one venture capitalist

Net equity position, % of GDP





Summing up

- Similar economic weight
- East Asia more heterogeneous, more open to trade
- East Asian integration into global finance increasing fast
- Europe champion of internal integration, North America lacks momentum, East Asia on dual track



Bilateral linkages Trade

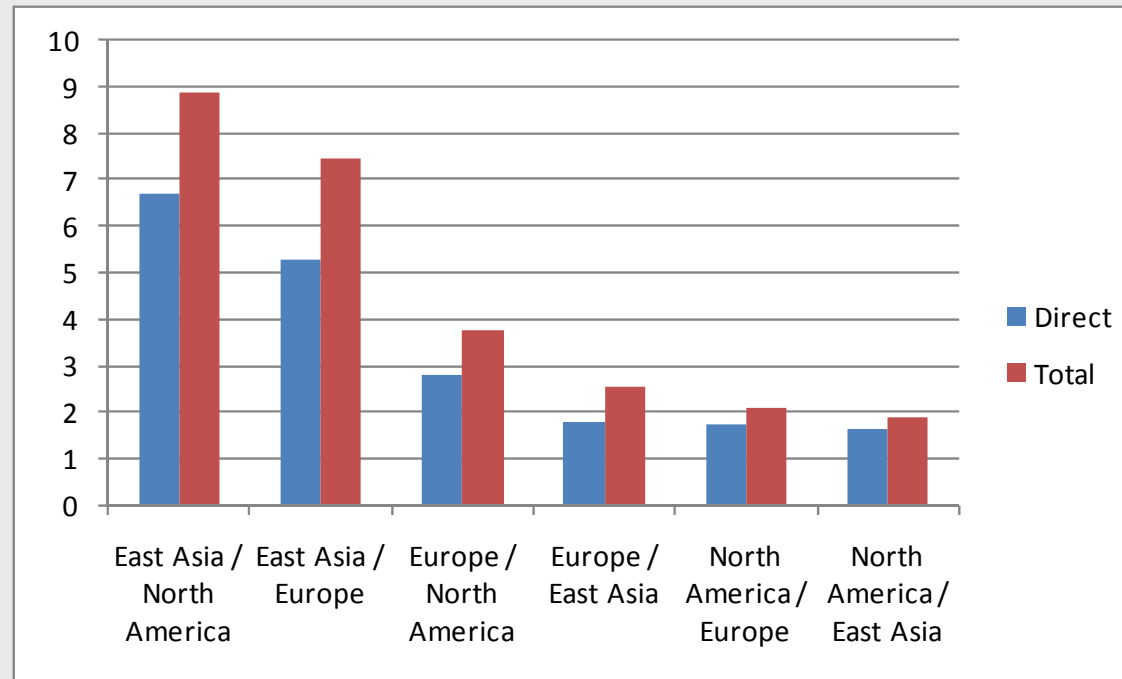
Bilateral trade links in percentage of the region's GDP

| Trading partner | East Asia | Europe | North America |
|----------------------|------------|-------------|---------------|
| Region | | | |
| | | 1996 | |
| East Asia | | 5.1 | 6.9 |
| Europe | 3.8 | | 3.7 |
| North America | 5.5 | 3.9 | |
| | | 2006 | |
| East Asia | | 8.1 | 9.4 |
| Europe | 5.2 | | 4.6 |
| North America | 6.6 | 4.6 | |



Export dependency

Direct and indirect export exposure, % of GDP





Bilateral linkages Finance

| Partner | East-Asia | Europe | North-America |
|----------------------|-------------|-------------|---------------|
| Region | | | |
| | | 1996 | |
| East-Asia | | 24.1 | 32.6 |
| Europe | 18.1 | | 53.4 |
| North-America | 27.0 | 58.9 | |
| | | 2004 | |
| East-Asia | | 43.5 | 60.0 |
| Europe | 27.4 | | 92.4 |
| North-America | 38.3 | 93.6 | |



Bilateral holdings

Strong asymmetries:

- East Asians hold American debt
- Europeans hold American equity and debt
- Americans hold European equity and loans

| | East Asia | Europe | North America |
|-------------------------|-----------|------------|---------------|
| | 2004 | 2004 | 2004 |
| East Asia | | | |
| Total assets (% of GDP) | X | 25 | 41 |
| Share of: | | | |
| Equity | | 19% | 14% |
| Debt | | 22% | 30% |
| Loans | | 35% | 14% |
| FX reserves | | 23% | 42% |
| Europe | | | |
| Total assets (% of GDP) | 12 | X | 48 |
| Share of: | | | |
| Equity | 45% | | 41% |
| Debt | 1% | | 26% |
| Loans | 53% | | 29% |
| FX reserves | 1% | | 4% |
| North America | | | |
| Total assets (% of GDP) | 12 | 45 | X |
| Share of: | | | |
| Equity | 71% | 60% | |
| Debt | 3% | 4% | |
| Loans | 23% | 35% | |
| FX reserves | 2% | 1% | |



Summing up

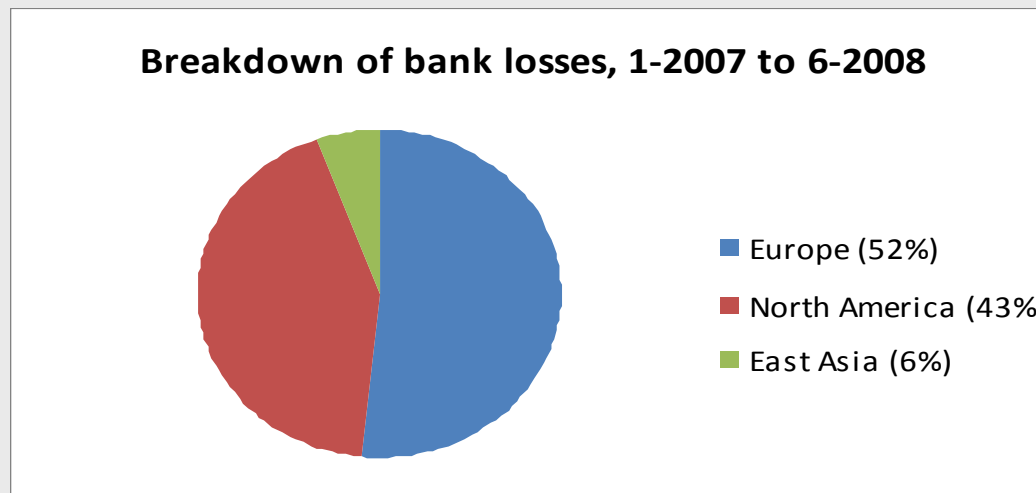
- A better picture of the world economy





3. Implications for shocks and adjustment

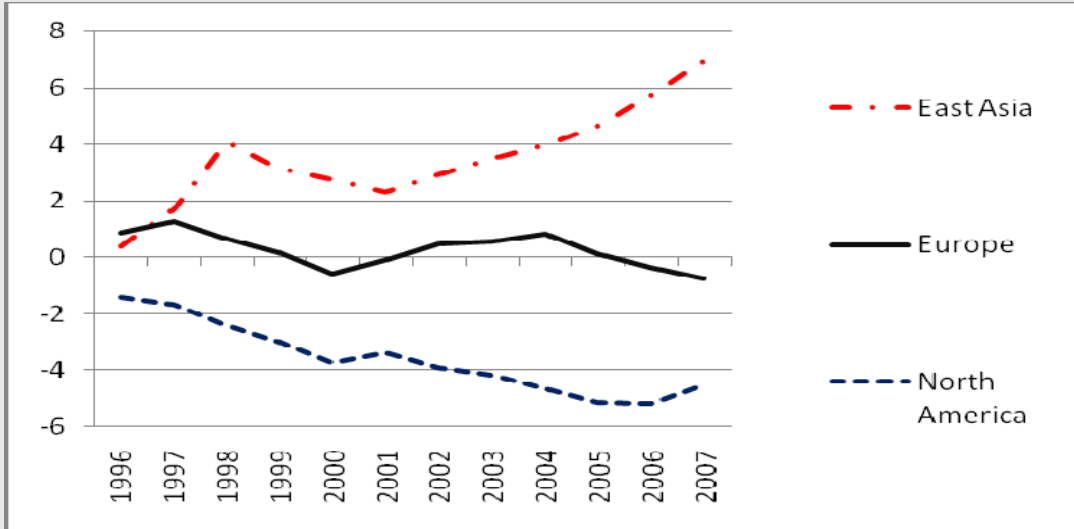
- **Demand shocks**
 - Asia clearly not a good candidate for decoupling, Europe more so
- **Financial shocks**
 - Transmission from North America to Europe, marginally only to East Asia





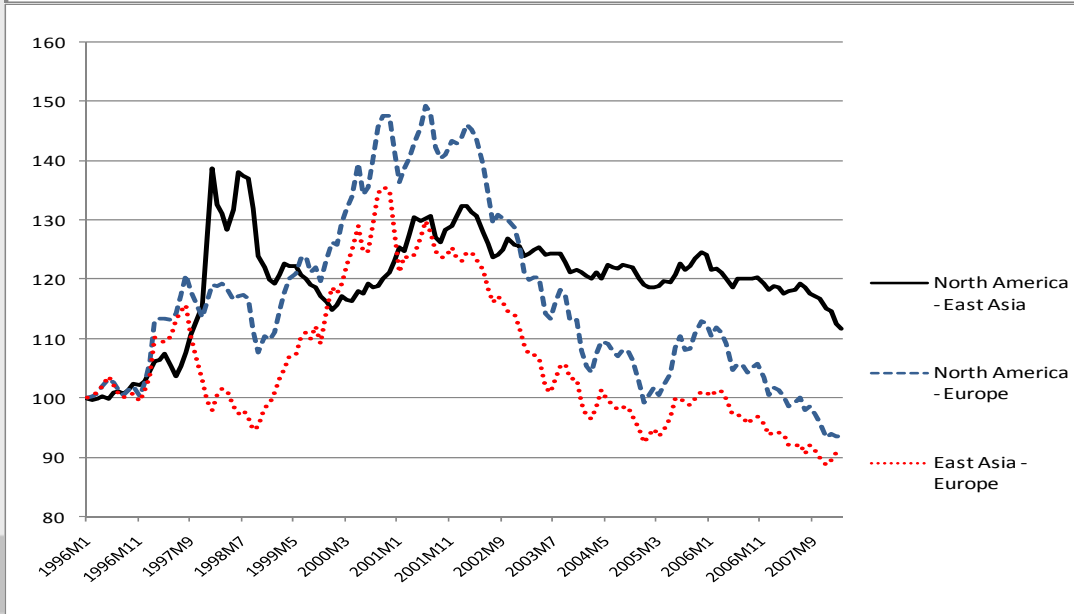
Global adjustment

The European paradox



- Europe as a bystander

VS.



- Europe at the forefront



European views on Asian exchange rate adjustment

- Long indifference / ambiguity
- Why?
 - Europe not part of the problem?
 - Uncertainty about effects on Europe (lower or higher exchange rate?)
 - Issue of time preference



Wealth transfer effects of exchange rate changes

- Valuation effects have become sizeable (even more so as data are for 2004)
- Wealth effects of North American depreciation significant for Europe, East Asia
- Motive for joint concern

Table 9: Variation in NFA/GDP ratios following a 10% North American depreciation

| | East Asia | Europe | North America | Total |
|---------------|-----------|--------|---------------|-------|
| East Asia | 0.0% | 0.4% | -3.4% | -3.0% |
| Europe | -0.3% | 0.0% | -2.6% | -2.8% |
| North America | 0.9% | 2.5% | 0.0% | 3.4% |



Conclusions

- Regional and global integration appear to be complementary rather than substitutes
- Why so little financial integration in East Asia?
- East Asia more dependent on developments in the rest of the world
- Transatlantic link has become second-order for trade, remains first-order for finance
- Europe's long-term interest is that East Asia appreciates
- Wealth effects point to joint interest in limiting dollar depreciation



Thank You For Your Attention

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