EUSI
EU Studies Institute

Working Paper Series E-2013-01

Lessons of the Euro Crisis: A New Asian Financial Order?

-From Japan's perspective -

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The Author thanks the valuable comments by Professors Hungdah Su, Chin-peng Chu, Toshiro Tanaka, Maxim Bouev, Yulia Vymyatnina, Irina Kuznetsova-Morenko,Chiaki Moriguchi, and all the participants of Asian Pacific Round Table on the European Union Studies – 2013.1.29-30 Hualien,Taiwan

Abstract

This article examines the lessons of the Euro Crisis for Asia, regarding the various short-term and long-term measures and the frameworks for coping with the crisis in the region, especially in the financial sector. Short-term measures need to be taken urgently, but medium and long-term measures should be realized in reliable, self-enforcing institutions, thus it is essential to analyze them based on an insititutionalist approach, rather than an intergovernmentalist approach.

In the Euro Crisis, both short-term measures and medium-term measures have been implemented mainly by European institutions, namely the EU and European Central Bank (ECB). In Asia, on the other hand, urgent short-term and measures were implemented mainly by the IMF and other supernational institutions. In Asia, such short-term measures continue to exist and evolve as various frameworks such as the Chiang Mai initiative, which was also effective for preventing the contagion from the Lehman shock and the Euro Crisis, which later spread on a global basis.

Still, in Asia, an overall framework or institution to cope with a regional crisis is required, as the Chiang Mai initiative is, even though it has been enforced and widened since the time of the Asian Crisis, merely a safety net agreed and maintained by the central banks in ASEAN + 3.

In order to establish such effective institutions to prevent a regional crisis, discussion on economic integration among the governments of ASEAN + 3 and other regional actors is essential, based on political stability among ASEAN +3 nations. Japan should naturally contribute to such discussions to establish effective institutions for such purpose.

Keywords: Euro Crisis, Asian Financial Crisis, institution, safety net, Banking Union, EU - Japan Relations

Introduction

In Europe, when the Greece Debt Crisis broke out in Autumn 2009, the price of Greek government bonds plummeted. The shock spread first to the small countries, Ireland and Portugal, then, as the serious situation continued, to some medium and large countries such as Spain, Italy and even France. The situation continued to worsen for at least three years, until the EU and European Central Bank announced measures that

seemed to be effective in Autumn 2012.

In Asia, the Asian Financial Crisis broke out in 1997 in Thailand, in the form of the sudden fall in the foreign exchange rate of the Thai Baht against major currencies. Then the crisis spread to Indonesia, the Philippines, Malaysia, then finally to almost all ASEAN countries and Korea, until these countries were eventually saved by a rescue package of the IMF and other organizations.

What are the differences between these two crises and what important lessons can be learnt? As has already been mentioned, the European crisis started in government bond markets and the ASEAN crisis started in the foreign exchange markets. The EU and European Central Bank (ECB) played the major role in rescuing the countries in trouble in Europe, even though the IMF worked jointly with them, on the other hand in Asia, the IMF played the major role.

In this article, for closer comparison, the measures to overcome the crisis are divided into two categories according to their different characteristics: short-term and medium to long-term measures. To be effective, short-term measures should be implemented quickly and effectively and the content of such measures should go beyond the expectations that prevail among the key actors in global society, both politically and economically. In order for the medium to long-term measures to be effective, the institutions affected by the proposed measures should be both credible and sustainable. Such institutions should continue to exist and develop, growing in credibility, both politically and economically.

In this article, first we discuss the background to and the reasons for the European Crisis, and then we examine the measures to cope with the crisis, both in the short-term and medium-long-term. Second, the Asian Crisis is discussed in a similar manner. In conclusion, the measures taken for both crises are compared and implications are made regarding which measures should be taken in future. The previous efforts and contribution of Japan to solve the crises, and the possibilities for the future, especially in Asia, are also discussed.

The Euro Crisis: How it occurred and worsened

In Autumn 2009, the newly elected Greek government announced that the previous government had hid a huge fiscal deficit. Although the deficit had been known about in Europe and there had been severe criticism especially from major countries such as Germany, It was an unexpected shock for global society, especially for global financial markets. This revelation triggered the Euro Crisis, which is still continuing.

There are considered to be two reasons why the Euro crisis has lasted so long: First, the crisis led to a so-called vicious circle, or vicious 'triangle,' composed of three factors, the deterioration of the economic situation in the Eurozone, the fiscal crisis, and the financial crisis (Bekx 2012). After the Lehman shock in September 2008, the Eurozone

economy was seriously affected by global factors including a decrease in exports from the Eurozone. Then, in response to such economic deterioration, the fiscal expenses of the Eurozone governments increased, on the one hand, almost automatically to pay for the increased cost of social security, for example unemployment insurance, and on the other hand, by the discretionary increase of expenses decided by the Eurozone governments, especially that by the countries in trouble. Such increases in fiscal expenses lead to an increased supply of government bonds, which worsened the environment of the Eurozone government bond markets. At this stage, the balance of supply and demand in the markets worsened. Bond prices fell sharply, in other words, bond yields went up. Then there was widespread fear in the markets that the fiscal situation would not improve in some countries, such as Greece, since the plans to decrease the fiscal deficits announced by the governments were not credible.

The decrease in the bond prices of such countries was always larger than that of Germany, which is considered to be the economically 'safest' country in the Eurozone. At this stage, the divergence between the yields of Greek government bonds and that of German government bonds, which has been the *benchmark* of the Eurozone bond market, widened.

What were the results of such instability? First, it naturally increased the costs of funding for the Greek government, which had a further negative effect on its fiscal balance. Since the cost of raising the money for income continued to increase, it was more and more difficult for the troubled countries to improve their fiscal balances. Second, the instability began to spread to other small countries such as Portugal and Ireland, which have relatively small economies in the Eurozone, then later to the relatively large economies of Italy and Spain, through the intensified anxiety of investors. This spread of the crisis is called contagion. Third, not only Eurozone investors but also global investors, who had invested in Greek and other countries' government bonds became worried about the fiscal situation of these countries and decided to withdraw their investments. The above-mentioned situation as a whole is called the fiscal crisis.

Then, the fiscal crisis caused the financial crisis. In Europe, most banks hold government bonds as assets, especially those of their own countries. This phenomenon still existed even though the Eurozone financial markets had become more integrated since the introduction of the Euro in 1999. In addition, the feeling of *home bias* remained by which European banks tend to invest in their own country's government bonds, as the banks consider themselves better informed regarding the condition of their own country's government bonds than the condition of other countries' government bonds. At the same time, major banks in the Eurozone, especially in large countries such as Germany and France, expanded their holdings of government bonds since the introduction of the Euro, not only of their home countries but also the small and

peripheral countries such as Greece. This was mainly because the exchange rate risk from such holdings was eliminated in Eurozone markets and the yields of the government bonds of small countries such as Greece were normally higher than those of Germany and France, reflecting the fiscal situation of such countries, which means the investors of the government bonds of small countries achieved lower risks and higher profits. But when the fiscal deficit measured in GDP for Greece became worse than expected, investors suddenly changed their minds and decided to withdraw their investments in Greek government bonds. This had a further strong negative effect on the price of Greek government bonds. In other words, the fall of the price of Greek government bonds was accelerated by the decisions of investors. Then the fall of the price spread to other government bonds, those of Ireland, Portugal, and Italy and Spain. The fall in the price of the bonds also affected the value of the government bonds that remained as assets of banks in the Eurozone. They suffered from a huge evaluated loss of assets. At this stage, the *fiscal* crisis caused the *financial* crisis in the Eurozone.

Finally, as the financial crisis deepened, the European banks become increasingly reluctant to lend money to corporations and industries because the losses the banks incurred from the Greek bonds worsened their financial results and made them more risk adverse. As a result, the CEOs of the corporations in the Eurozone became increasingly pessimistic toward making new investments in their factories etc. and the corporations became less active due to the restrictions in the money supply from banks. This caused a vicious circle in the Eurozone, with further deterioration of the economic situation, the fiscal crisis, and the financial crisis

What measures were taken to halt this vicious circle and what measures could have been taken? In answering these questions, the strict and negative attitude of Germany together with some other rich countries in the Northern Eurozone, such as Finland and the Netherlands should be considered. Since the Greek fiscal problem was revealed in Autumn 2009, the discussions on how to cope with this issue continued on an EU level and could not reach a fruitful conclusion until May 2010, when the heads of state or government of the Euro area decided to implement a support package for Greece jointly with the IMF (European Commission, 2010).

Urgent measures taken by the EU and the ECB

During the six months from Autumn 2009, discussions on an EU level continued, but reached only partial or minor results due to the strong reluctance of Germany, and such outcomes were always behind the expectations of the financial market participants who wished to obtain relief from the EU and the IMF on their holdings of Greek government bonds.

Why has Germany been so strict regarding the rescue of Greece? The former Greek government had hidden the fiscal deficit for a long time and this was known among

countries including Germany, who doubted the capability of Greek political leaders. At the same time, Germany has a long-standing dislike of inflation, due to their previous experiences of hyperinflation. As a generous fiscal policy may lead to inflation by increasing the expenses of governments, *fiscal discipline* is a key pillar of German economic policy. Such German idea was reflected in the Maastricht Treaty, especially in the Maastricht Criteria, which determines the conditions for becoming a member of the EMU, on inflation rates, fiscal balance, fiscal deficit, long-term interest rates, and exchange rate stability. So if a country such as Greece passed the Maastricht Criteria, became a member of EMU and then widened its fiscal deficit and asked other Eurozone countries for help, it would be regarded as 'a free rider,' which had enjoyed the economic benefits accruing from the increased fiscal expense but tried to avoid the higher cost of funds or cutting their fiscal budget. Otherwise the countries in trouble, not only Greece but also other countries, which might have similar problems, would create a *moral hazard,* under which they had the expectation of being saved whenever they had a fiscal problem. In addition, among German citizens, general dissatisfaction mounted that the money that German citizens paid as tax to their government should not be transferred to problem countries such as Greece. Prime Minister Merkel and other German politicians should have understood the importance of the role of Germany in solving the crisis on an EU level, but at the same time they could not neglect the opinions of German citizens, especially at the time of elections.

Based on this background, such strict attitude of Germany continued even after this first rescue package of May 2010 was announced. A typical example is the strong opposition of Germany to the idea of *Eurobonds* issued based on the creditworthiness of the EU as a whole, including Germany. It was proposed by the European Commission in 2011, but has not been approved finally by the Council of the EU. The current balance of the Eurozone as a whole has been approximately balanced. On the other hand, the current balances of the Eurozone countries have become increasingly divergent, for example, between that of Greece and Germany. This was contrary to the expectations at the start of the EMU in 1999, that is, the current balances among the Eurozone countries were expected to converge once the single currency had been introduced. The divergence may have widened because competition in the various industries strengthened the market leaders in the single market with one single currency and there was almost no mechanism to compensate for this discrepancy, such as the redistribution of fiscal policy covering the EU, which includes the whole Eurozone. In order to compensate for such discrepancy, a Eurobond might have been useful, but Germany opposed the idea insisting that it may cause Greece and other troubled countries to rely too much on the scheme.

When urgent measures for the crisis were introduced by the EU, pressure on the ECB mounted because the ECB had to cope with the crisis as the stability of the European

financial markets, not only the bond markets but also the stock markets and foreign exchange markets, and it had to develop measures to recover such situation. Since Mario Draghi was nominated as the president of the ECB in November 2011, he started to implement effective measures to stabilize the financial markets. In other words, President Draghi decided to take several measures that exceeded the expectations of the financial market participants. First, the ECB decided to implement the long-term repurchase operation (LTROs), by which it would supply money for 3 years, which is an unprecedently long time, to the financial institutions in the Eurozone twice, in December 2011 and February 2012. Banks in the Eurozone were relieved as they could raise the money easily at lower cost from the ECB. A large portion of the money was allocated through the balance sheets of Eurozone banks to invest in government bonds, including those of Italy and Spain. Second, the ECB enforced the facility of purchasing the government bonds. It started the Security Market Programme (SMP) for the first time in May 2010, at the same timing that the EU and the IMF decided the first rescue package for Greece. Since it was not sufficient considering the deteriorating fiscal situation of Greece and the contagion to other countries, especially to Spain, the ECB announced that it would start an unlimited purchase facility of Eurozone Government Bonds: Outright Market Transactions (OMT). These two measures, providing long-term money to financial institutions and the unlimited purchase of government bonds, exceeded the expectations of financial market participants at each announcement. In this sense, they were effective measures to cope with the crisis. Still, they were urgent, temporary measures to recover from an irregular, unstable situation of the financial markets, and designed only for the short-term. In addition, their remarkable result at the first stage was based on the surprise of the market participants at the announcements. Therefore as time passed, such positive effects diminished. They did not remove the substantial causes of the crisis. In other words, they did not halt the vicious cycle, which is composed of the fiscal crisis, the financial crisis, and the slowing economy.

New Framework of the EU: Is It an Institution?

Then, what are the necessary conditions for solving the crisis in the long-term? The establishment of a permanent framework is a necessary condition but may not be a sufficient one. For example, the European Financial Stability Facility (EFSF) was established on the occasion of the first rescue package for Greece in May 2010, as a temporary framework. It was supposed to be transformed to the European Stability Facility (ESM) as a permanent framework, scheduled to start from July 2011. Even though there was a delay in its establishment, due to an argument in Germany, the ESM was established in October 2011. But will its establishment immediately work to

improve or solve the crisis in Europe? Even if the ESM has been acknowledged to work by the financial market participants at the start of the establishment, will it continue to work in the same way from now on?

In order to answer these questions, we should refer to the theory on European Integration. There have long been discussions between intergovernmentalists and neo functionalists. The former assumes the sovereignty of the countries even when they negotiate opportunities on integration. On the other hand, the latter stresses 'how spillover processes and the autonomous actions of super rational actors (including the Commission and European Court of Justice) contribute to European policy making' (Pierson, 1996)[1]. In this article, we rely on *historical institutionalism* that, according to Pieson's paper, 'actors may in a strong initial position, seek to maximize their interests, and nevertheless carry out institutional and policy reforms.' We rely on historical institutionalism because it understands the integration as a path-dependent process 'in which initial institutions or policy decisions can become self-reinforcing over time' (Pierson, 1996).

It is especially applicable to the analysis of the institutions and policies in Europe, which will be developed for the long-term, not only to cope with the present crisis but also to prevent a crisis that may occur in future and cause a problem for the European integration process. The institution built for European integration should be self-reinforcing, in other words, credible and robust over time, facing the expectations of financial market participants, which may change from time to time.

Having these discussions in mind, we next examine what has been decided in the EU and how the institution for the further integration process will become credible for the long-term.

First, at the European Council in June 2012, it was decided to develop 'a specific and time-bound road map for the achievement of a genuine Economic and Monetary Union.' Under this agenda, the Council clearly decided to take the measures of the Banking Union, which are composed of three frameworks, the Single Supervisory Mechanism (SSM), the Single Resolution Mechanisms, and the Deposit Guarantee Mechanisms.

It was a turning point in EU policy and a step toward building up frameworks for further integration of Economic and Monetary Union. Under this decision, the European Council announced clearly that, among the three factors of 'the vicious cycle,' the financial crisis should be tackled by the Banking Union, before the other two factors, the fiscal crisis and the slowing economy, in order to pave the way for the longer-term integration. In other words, the European Council took a realistic approach to cope with the financial crisis first, as it was already found difficult to solve the fiscal crisis directly,

1. The analysis of institutions is an area of overlap between Politics and Economy, especially when the focus of analysis is on the historical development of institutions (Pierson, 1996).

either by the issue of Eurobonds to allocate money to countries in the Eurozone or by the efforts of respective countries in trouble to recover from the fiscal deficit. Concerning the three measures of the Banking Union, the Single Supervisory Mechanism (SSM) was understood as the top priority. This was because, first, only after the Single Supervisory Mechanism was realized, was the direct recapitalization of banks supposed to be possible, which will be an effective way to stabilize the financial sector in the Eurozone, without affecting the fiscal balance of the country where the problem banks are located. Second, the European Central Bank (ECB) is acknowledged as a credible actor that has various measures to stabilize the financial markets, not only in the Eurozone but also on a global basis.

After several discussions, on 5 December 2012, the so-called 'Blue Print' was proposed by President Herman Van Rompay of the European Council. It was officially titled 'Towards a Genuine Economic and Monetary Union'[2]. It was basically agreed later as the roadmap for the completion of EMU, in one part of the Conclusions of the European Council on 13/14 December 2012. The Blue Print specified the three stages as the time framework: Stage 1 (End 2012-2013), Stage 2 (2013 – 2014) and Stage 3 (post-2014). At the same time, three main policy areas were mentioned, corresponding to each factor of the vicious cycle of the crisis, an Integrated financial framework, Integrated budgetary framework, and Integrated economic framework. In this way, the time schedule for three policy areas was specified. According to this time schedule, the Integrated financial framework should have priority. Most works on this area should be done in Stage 1 and Stage 2. In particular, 'it is imperative that the preparatory work can start in earnest at the beginning of 2013, so that the SSM can be fully operational from 1 January 2014 at the latest' and under such time schedule 'the legal and operational framework for ESM direct bank recapitalization should be finalized by the end of March 2013' (Van Rompuy, 2012). In addition, 'the SSM will need to be complemented by a single resolution mechanism, as well as more harmonized deposit guarantee mechanisms,' and the proposal for these two other mechanisms than the SSM is supposed to be agreed at Stage 1, later specified 'until June 2013 ' by the European Council. On the other hand, in the other two policy areas most tasks should be done in Stage 2 and Stage 3. Concerning the Integrated budgetary framework, in spite of some additional frameworks (so-called 'two-Pack ') that strengthen the fiscal discipline of the Eurozone countries, the two new frameworks will be realized later; Financial incentives linked to contractual arrangements at Stage 2, which provides the incentives, based on the mandatory agreements for Eurozone countries, to the countries that make efforts to

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2. In the Blue Print, Political Accountability is mentioned as the fourth policy area, which we do not discuss in this article. Throughout the three stages,' Commensurate progress on democratic legitimacy and accountability' are planned.

improve their fiscal discipline, and country-specific shock absorption at Stage 3, which includes the setting-up of risk-sharing tools called Fiscal Capacity, a kind of common fund to absorb such shocks. In the area of Integrated economic framework, in addition to the framework for the ex-ante coordination of economic policy reforms that exist, the arrangement of the surveillance for the coordination assumes the development of frameworks in other policy areas, especially the Integrated budgetary framework. Therefore it will be implemented basically at Stage 2 or later.

In this context, the initial plan of institution, including the time schedule, has been set in December 2012. Step-by-step measures will evolve based on the accumulation of the results of the three policy areas, in other words, from Banking Union to Fiscal Capacity. Based on such initial setting, the new institution of the European Integration will evolve as a self-enforcing, robust one depending on the interaction between the implementation of the EU on announced at the initial stage and the response from the external environments, either positive or negative, especially from financial market participants.

Asian Financial Crisis: The development of a safety net

The Asian Financial Crisis broke out first in July 1997 in Thailand, spread to Indonesia, the Philippines, then finally to almost all ASEAN countries and Korea, by the end of the year. It is not necessary here to follow the whole story of how the Asian Financial Crisis happened, deepened and finally resolved, but to describe interesting points for comparison with the European Crisis.

First, the Asian Financial Crisis led to a sharp depreciation in local Asian currencies in the foreign exchange markets, starting from the sudden depreciation of the Thai Baht. The background to such movements in the financial market was that the pegging of the Thai Baht to the US dollar, the international currency, lost its credibility. At first, the inflows of money sustained the pegging of the Thai Baht to the US dollar, but when the inflows of money continued and flowed from the banking sector to the real estate markets, real estate prices became irrationally high. Then the foreign market participants decided to withdraw their investments from Thailand. On the other hand, the start of the Euro Crisis was the sharp decrease in the price of Greek government bonds. The Greek fiscal deficit triggered the crisis and there was almost no other way for financial market participants to react, since Greece had adopted the Euro, the single currency. Generally, foreign exchange markets are more volatile than government bond markets, since the flow of money in the former moves in the shorter-term than in the latter. Still, at the time of the respective crises, both Thailand and Greece relied on inflows of money from overseas market participants, who decided to withdraw their investments, causing a serious shock in both markets. The crisis became contagious in both cases for similar reasons as financial market participants became increasingly

anxious. In Europe, the crisis spread from Greece, to the government bond markets of Ireland, Portugal, Italy and then Spain. In Asia, the crisis spread to the forex markets of Indonesia, the Philippines, Korea and most other ASEAN countries.

The second question was: who were the actors who arranged the rescue package to cope with the respective crises? To cope with the Euro Crisis, it was mainly the EU and the ECB who implemented urgent measures. The IMF also contributed, but they acted basically in collaboration with the EU and the other European actors, as was typically seen in the arrangement for the rescue packages of Greece. On the other hand, the IMF arranged the urgent rescue package and planned the economic policy regime for each Asian country in trouble. Still, some measures were taken based on the ASEAN regional framework. The setting up of the Asian Monetary Fund (AMF), which Japan principally worked to establish, was finally not successful, due to the objection of the US (Gilson, 2000). Later in May 2000, the Chiang Mai Initiative (CMI) was agreed, 'which is the network of bilateral currency swap agreements among ASEAN +3 (Japan, Korea and China) countries, to address short-term liquidity difficulties in the region and to supplement the international financial arrangements.' In the same way, the Asian Bond Market Initiative (ABMI) and the regional surveillance on economic policies started, but the Chiang Mai Initiative (CMI) has been the main pillar of policy on the Asian level to cope with the Financial Crisis.

Is the Asian Financial Order and Economic Integration developed?

We have already examined how the long-term framework for coping with the crisis in Europe will be built. How about in Asia? In addition to the short-term measures taken in Asia, which are mentioned in the previous paragraph, what long-term framework has been developed for an institution to prevent a future crisis in Asia?

First, the framework of the Chiang Mai Initiative developed and worked efficiently in order to prevent the crisis or prevent the contagion of the crisis, from external shocks such as the Lehman Shock or European Crisis. In other words, it originally started as a crisis facility and then developed as a permanent facility to prevent a future crisis in Asia. In line with this development, the multilateralization of CMI (CMIM) started, in which bilateral swaps were converged to multilateral swaps, and at the same time the total size of the facility increased (Park, 2012), in order to strengthen its effectiveness in the financial markets.

Second, the Asian Bond Market Initiative (ABMI) started and developed. It is based on the idea that one of the reasons why the Asian Crisis was so serious was that the banking sector was too dependent on Asian financial markets. Asian banks, typically in Thailand, received huge inflows of money from outside the country and arranged loans too easily to inefficient sectors such as the real estate sector. As the banks' evaluations of borrowers became overly generous and the loans seemed unlikely to be repaid,

overseas market participants started to worry about the situation and retreat from lending money to Asian banks. If the bond markets had been developed, the investment behavior might have been more rational, as investors would know where their investments had been allocated and the details of the investments. Based on these discussions, new frameworks of the Asian Bond Market Initiative (ABMI) were developed by the finance ministers of ASEAN+3, leading to the Asian Bond Fund (ABF) starting from 2003, which invests sovereign and other kind of bonds, and the ASEAN + 3 Bond market Forum, which coordinates the regulations of bond markets in Asia and other issues (Park, 2012). Still, the development of bond markets in Asia is an ongoing and gradual process.

Third, regional surveillance of economic policies was also being considered at the time of the crisis through the Economic Review and Policy Dialogue (ERPD), in relation with the Chiang Mai Initiative. Such frameworks on regional surveillance of the economic policies of ASEAN + 3 countries continued and the Regional Comprehensive Economic Partnership (RCEP) is under discussion to improve economic integration through active trade and foreign direct investment until 2015 (METI, 2012). Still, on this issue of economic surveillance or integration on economic policies, the ASEAN +3 area can be divided into two areas, ASEAN and Eastern Asian Countries, Japan, Korea and China.

Among the ASEAN countries, such discussions have been held for a long time, which should become a base for all ASEAN+3 regions. On the other hand, among the three Eastern Asian Countries, economic integration through active trade and foreign direct investment has been on the agenda but discussion has been hampered by political issues, especially on the island territory issues, between Japan and Korea, and between Japan and China. Therefore the success of RCEP will largely be based on the integrated framework that has been achieved up to now in ASEAN and the important question will be how far the three Eastern Asian Countries, Japan, Korea and China, will participate in the discussion positively and flexibly.

Of the Chiang Mai Initiative, the Asian Bond Market Initiative (ABMI), and the Regional Comprehensive Economic Partnership (RCEP), the Chiang Mai Initiative has worked not only as a framework, but also, afterwards it has continued to develop and strengthen its functions, it has been working as a permanent framework to prevent crisis in the region. The other frameworks are still under development.

Even though the Chiang Mai Initiative has become a permanent framework, because its function is to provide funds to problem countries it will be useful to prevent or cope with a financial crisis, especially caused from outside the area, but it will not necessary survey and correct structural problems caused inside the area.

Why is the present situation of the framework in Asia like this? First, although the Asian countries suffered economically from the Financial Crisis, most of them recovered strongly, because they are rapidly developing countries with high quality labor forces

and relatively low costs and also because the depreciation in their currencies during the time of the crisis contributed to the recovery of their export thereafter. So it was not essential for the Asian countries to discuss a further integration process, especially involving the coordination of economic policies.

Second, the political disputes, especially in East Asia, hampered progress in discussions on the integration process. Also, the discussion on the Asian Currency Unit (ACU), which would pave the way for the Asian single Currency, was hampered by the dispute on the initiatives in this area among the three countries in East Asia.

Even though the Chiang Mai Initiative has a successful framework, it should be reinforced by the other frameworks for the capital markets and the economic policy surveillance in the region. These frameworks as a whole, may work as institutions that are sufficiently credible and self-reinforcing to prevent the crisis and contribute to the further integration process in the region.

The implications for the role of Japan

Finally, as an appendix, we discuss the implications for the role of Japan, to contribute to the stability of both the European and the Asia regions.

First, concerning the short-term measures to cope with the Euro Crisis, Japan contributed directly and indirectly. Directly, 'Japan has been purchasing European Financial Stability Facility (EFSF) bonds.' In addition, in January 2013, the Japanese Ministry of Finance announced the purchase of bonds issued by the ESM. Indirectly, 'Japan has been working through the IMF,' for example 'Japan assigned $100 billion to strengthen the firewall after the Lehman shock and Japan signed a $100 billion Borrowing Agreement with the IMF in February 2009 ' and 'the EU can use this money to support Euro member states in financial trouble' (Tanaka, 2012).

But as we argued previously, the EU and the ECB played the main role in coping with the crisis and from outside the Eurozone the IMF and major countries such as the US and Japan played a complementary role.

On the other hand, to strengthen economic relations between Japan and the EU / the Eurozone for the long-term, discussions on a FTA between the EU and Japan were started in November 2012 in the EU[3]. Even though there is opposition on both sides, for example the agricultural sectors in Japan and the automobile sectors in some countries in the Eurozone, it will pave the way for a new era in economic relations between Japan

3. The FTA negotiation between Japan and the EU is an important issue that remains to be discussed on another occasion. Japan's positive attitude towards a FTA with the EU has been largely affected by the already existing FTA between the EU and Korea. As the industrial structure of Japan and Korea similar, in that their industries both concentrate on the automobile and electronics sectors that the FTA between the EU and Korea has been very beneficial for Korean companies compared to Japanese companies.

and the EU. The main issues have been the series of trade conflicts since World War II. While overall agreements to collaborate proved ineffective, such as the Action Plan based on the Hague declaration in 2001 (Berskofsky, 2012), the FTA may improve economic relations between Japan and the EU substantially.

Next, on the measures to cope with Asia, even though there has been some criticism especially from Europe, that Japan did not contribute to the recovery of the EU from the crisis, the Japanese government did make various efforts to contribute to the recovery of Asian countries, in addition to the plan of the Asian Monetary Fund (AMF), the Chiang Mai Initiative and Asian Bond Initiative (ADBI) as already mentioned (Gilson, 2001).

In the long-term, the key question will be how Japan can contribute to the development of ASEAN + 3 as a credible, self-enforcing institution. Toward this end, how Japan will work intensively toward the RCEP, as has already been discussed, in which the coordination of economic policies are supposed to be discussed and the integration of the internal markets in Asia, will be the key issue. In this regard, considering the difference in the stage of economic development in Asian countries, it is prudent to develop *bilateral* discussions between the countries in Asia on the FTA and the development of FDI.

Finally, in discussing this long-term framework, a comparison with ASEM is useful. An institution develops historically depending not only on the starting point but also on how its itinerary evolves. ASEM started between the EU and ASEAN+3 as an informal body in 1996, mainly for economic discussions. The economic miracle of Asia was already apparent in the early 1990s, so 'the rise of the economic potential of the Asian region and its growing markets attracted EU member states to participate in ASEM in 1996.' Directly afterwards, in 1997, the Asian Financial Crisis broke out. As a result, ASEM had become a useful framework for discussing how both parties should cope with the crisis. Based on these discussions, once the framework of ASEM was established, it worked as a multidimensional institution, 'devoting equal weight to political, economic and cultural issues' (Gilson, 2001).

Conclusion

In this article we discussed measures to cope with the crisis in Europe at present and in Asia in the 1990s.

First, we classified measures to cope with the crisis into two categories: short-term measures as an urgent remedy; and long-term measures to prevent a future crisis and strengthen the present economic and political frameworks. Second, we examined whether the long-term measures can develop to become established as credible and self-enforcing systems, as institutions that then develop historically.

Based on these two criteria, we analyzed the current situation, first in the Eurozone. Even though the European Crisis is still on going, the urgent measures to cope with the

crisis taken by the EU and the ECB have been effective. On the other hand, the long-term measures to achieve further financial, fiscal and economic integration are only just beginning, with decisions being made on the road map and further discussions towards the end of 2012.

Among the various short-term measures taken in Asia that were planned during the crisis in the 1990s, the most successful framework was the Chiang Mai Initiative, arranged among ASEAN+3 countries. Since the Chiang Mai Initiative is a framework to provide funds to member countries, it was useful not only to provide urgent short-term measures, but also for the long-term to prevent a future crisis. Therefore it was strengthened and developed. At the same time, it only covers the arrangement of providing funds to member countries and no further integration in ASEAN+3 has been developed. So in order for ASEAN +3 to become an institution, further discussions especially on the coordination of economic policies and the integration of markets in Asia are required.

Finally, as an appendix, we consider the implications of these discussions for the role of Japan, to contribute to the stability of the regions both in Europe and in Asia,
both for the short-term to help resolve the crisis and the coordination of economic policies for the long-term. In this regard, free trade discussions will be the key for Japan's relations both with the EU and Asia.

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