



# **Comments on “*Overinvestment in Asia*” by Wataru Takahashi**

**Presentation to the Reserve Bank of India and European  
Commission ASEM conference,  
"Investment and its Financing: What causes private  
investment to remain relatively low in Asia?"  
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## General comments

- Presentation questions presumption of conference.
- Agree, as did Olaf Unteroberdoerster, that over-investment is the more likely condition in China.
  - Eg, maglev train in China, not in Germany.
- But consider implications: Hobson's choice between:
  - Financial instability if credit in China grows fast enough to induce over-investment.
  - ROW has to absorb savings from large Chinese current account surplus if credit and investment grow at more reasonable rates.



## But overinvestment in ASEAN?

- As Deputy Governor Gokarn noted, Asia not homogenous.
- Corporate sectors running financial surpluses, long after balance sheet repair after the Asian financial crisis.
- Puzzling but part of a broader puzzle:
  - Corporate sectors in many countries, including China, running financial surplus.
  - But true in many industrial countries as well.



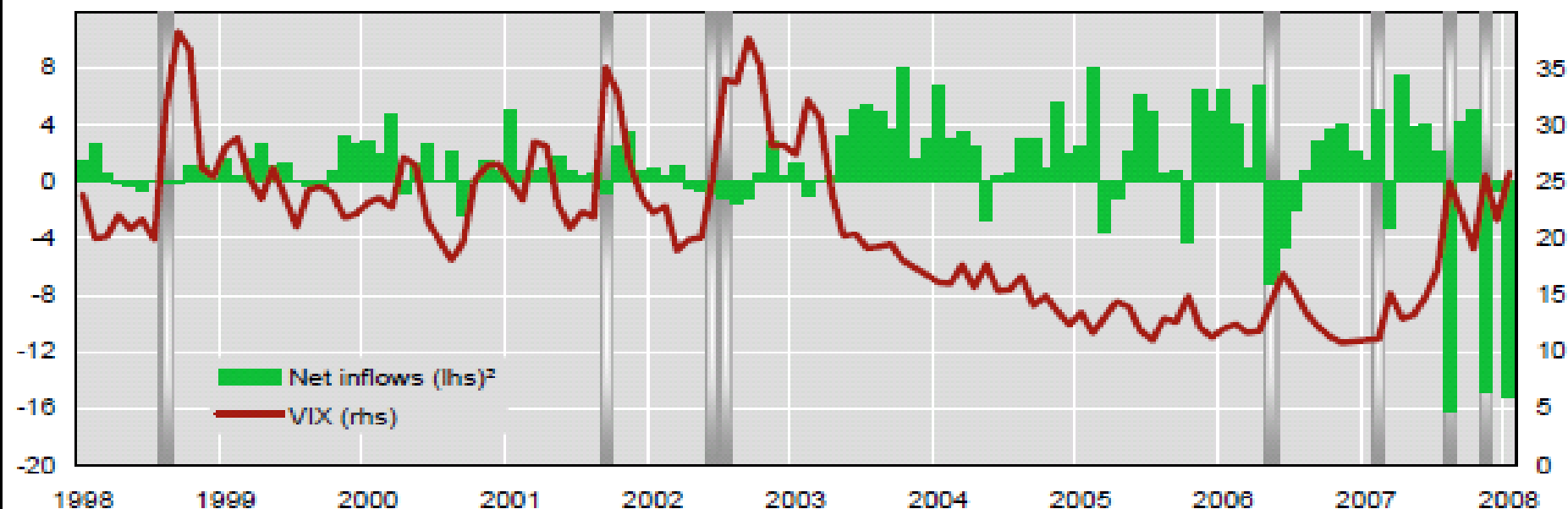
## Why are countries unwilling to run current account deficits?

- In India, could say generation that experienced reserves going to zero and the gold being pawned says never again.
- But a larger Pavlovian process is at work, with often painful consequences for countries that allowed their current account deficits to widen:
  - Latam in 1980s;
  - Asia financial crisis;
  - New EU members;
  - Deficit countries in euro area.



## VIX and portfolio equity flows to Asia

Figure 1: Global Volatility and Asian Net Equity Inflows<sup>1</sup>



Note: shaded areas refer to seven episodes of rising volatility since 1998: the Russian default (Aug 1998), September 11 (Sep 2001), June–July 2002, the May 2006 sell-off, the February 2007 sell-off, the Bear Sterns hedge fund woes in August 2007, and the subprime-related sell-off in November 2007.

<sup>1</sup> Net foreign purchases of equities in India (data start in 1999); Indonesia; Korea; the Philippines; Taipei, China; and Thailand. <sup>2</sup> In billions of US dollars.

Sources: Bloomberg; CEIC; Korean Stock Exchange; Philippines Stock Exchange; BIS calculations.



## Nature of international risk sharing?

- Textbook tells story of two similar islands at different latitudes that agree to exchange half their harvests.
- But global investors seek a call option on India's economy, and sell when global uncertainty rises.
- Indian economy asked to provide liquidity to global investors when VIX rises.
- Faced with such capital flows, what are prudent authorities to do?
- "Global imbalances" pose questions of the unobserved deficits as well as the observed surpluses.