ACHILLES' HEEL - CAUSE OF CURRENCY CRISIS

by VŨ NGỌC NHUNG

Regional financial crisis is not only a global disaster as it slashes many countries, but also it contains many puzzles. The depreciation of Japanese yen which recently led to an increase in U.S. dollar value though not higher as in the past, of currencies in countries incurring financial meltdown just from 1997 and especially 0.5 percent drop in Taiwan dollar in the second week of June 1998, 5% drop in Australian dollar in May - the lowest level within 12 past years - is a sad notice telling currency crisis has started its second phase and it will not release any country. The U.S. also fears it will suffer more trade deficit from Japanese imports because yen falls and Japanese goods become cheaper and American vulnerable point is a great number of American bonds worth US$500 billion in the Japanese hands. As a result, although some American censured proudly that Japanese economy is inferior to American one and Japanese management no longer dominates American one as in 1980s, but many American economists and business people warned if Japanese are badly in need of U.S.dollars to revitalize their economy and sell only one third of the above bonds, American financial bubbles will burst and disaster cannot be stopped. Recall when yen appreciated from Y250 to US$1 (in 1984) to Y128 to US$1 (in 1988), Japanese rushed into the U.S. to buy everything from Rockefeller's office buildings to small companies and used their managerial skill to produce profits from these entities. Today many American also want to do the same.

The forecast of the World Economic Forum held in Dovos, Switzerland in January 1998 that the third currency crisis (after Mexico and East Asia) would break out in Russia within 6 to 9 months has come true. Russian President Eltsin petitioned the world's US$15-billion aid to tackle the crisis. Russia and Brazil were top countries that the forum predicted their danger of financial mess because they had the same weakness as East Asian devaluation-hit countries. But even so-called strong economies cannot escape money storm. It is found most of the countries have Achilles' heels whereby currency crisis spreads.

The most destructible point is many famous economists and the International Monetary Fund - IMF intentionally or accidentally do not see harmful effects of speculation rising many times againt those of currency crisis, generated virtual economy. Virtual economy made many entrepreneurs and economic managers' mistakes in their policies. Looking at the faults triggering currency crisis, we can see the stamp of speculation and virtual economy:

- Borrowing great foreign loans mirrored virtual real estate prices. Take domestic examples to understand the virtual state of some countries: Some local companies such as Minh Phụng, Epco, Ngọc Thảo pursuited virtual housing prices they created by morgaging their virtual assets into banks for loans to boost the demand for speculation in properties. Foreign investment focused on office buildings also blowed the housing bubbles and made it more colorful. Every country experienced the fact that housing prices skyrocketed but dropped dramatically by 40%-50% resulting in collapse of real estate companies and banks involving in funds to housing business.

Opening deferred payment L/Cs worth US$1.2 billion and then some companies dumped their imported goods and poured proceeds in real estate business. Some countries likely read the articles saying about the risks of these deferred-payment L/Cs from late 1995 and early 1996, but they continued to give green light to opening fiduciary L/Cs, so foreign banks also mistook virtual with real things.

- Maintaining a fixed foreign exchange in years also showed illusions about the strength of local currencies.

- Great current account deficit, doubling the safe level permitted were also due to statistics that caused false balance.

- Uneven investment structure due to pursuing virtual profits in real estate business.

- Corporations and giants gained low return ratio but they still had illusions to keep it strong by the government interference.

- Some hedge funds by their short sale tricks blowed bubbles of demand for U.S. dollars up hundreds of times and widened the gap in dollar demand and supply in every currency crisis. Consequently, the price of U.S. dollar soared many times and dropped sharply by February 2, 1998 when speculators sold off US$500-600 million per day. Seeing the following table, no one can deny the role of that speculation, nevertheless the IMF failed to meet the East Asian countries' suggestion of control over global money trading in the meeting on Dec 31, 1997.

Speculation caused great fluctuations in currencies as mentioned above. If it had not taken shape, firms would not have gone bankrupt. So condemning only policy mistakes will make crisis incurable.

	Depreciation within 7 months	Appreciation	Within	Depreciation again in June 1998
Indonesia	600% from 2,500 to 15,000 rupiah/US$1	532% to 7,500 rupiah/US$1	20 days	From 7,500 to 13,000 rupiah/US$1
Thailand	118% from 25.5 to 54 baht/US$1	20% to 34 baht/US$1	10 days	From 34 to 44 baht/US$1
Singapore	26.1% from Sing$1.42 to 1.765/US$1	10.4% to Sing$1.62/US$1	20 days	
Philippines	66% from 2.65 to 4.25 peso/US$1	22.6% to 3.88 peso/US$1	11 days	
Malaysia	84.3% from 2.55 to 4.25 ringgit/US$1.	35% to 3.45 rinngit/US$1	20 days	From 3.45 to 4.01 ringgit/US$1

As such, if speculation is defended as innocent, it must be explained why the above countries mended their faults in economic management during a miraculous time from 10 to 20 days but they committed mistakes again and this time was only few months, not 5 to 10 years as before crisis. Speculation is allowed by many countries. The U.S. forbids only manipulation and permits speculation by law. It can be hardly imagined that speculation is separated from manipulation due to distortion of U.S. dollar demand and supply by short selling tens of billion of local currency and short buying billions of U.S. dollars in a day. This is just manipulation of U.S. dollar prices through demand and supply. The reform of the stock market after the Great Depression in 1929-1932 resulted in laws limiting speculation. It helped prevent the cyclic economic crisis in the anarchic capitalism. After the stock market downfall in 1987, there were also laws permitting the closing of the stock market in half a day, a whole day to ease the "sheep effect" caused by speculation. Nevertheless, after the East Asian money mess, the institution in charge of stabilizing international currencies, IMF, could not stop currency crisis and did not analyze the destructive role of speculation and failed to control money trading as proposed by regional countries. Saying the IMF do not understand how speculation boosted demand or it dare not struggle against thousands of hedge funds - haunting power of financiers - is a bias in favor of those who hunt profits by killing economies. I hope such vulnerable points should be identified■