Preface

Developing Asia is one of the most dynamic regions of the world economy, sometimes called "Factory Asia." The region, which encompasses a wide range of countries at different income levels, also varies widely in terms of financial sector development. Singapore and Hong Kong, China are international financial centers, many middle-income countries have a good mix of banks and capital markets, and in some low-income countries even banks, let alone capital markets, remain underdeveloped.

Although their financial development level varies, developing Asian countries as a whole have made significant strides in recent years. For example, the banking sectors of countries hit by the Asian financial crisis have become healthier due to extensive postcrisis reform. Another example comes from the People's Republic of China, which gave virtually every poor household a bank account ten years ago—to minimize the leakage from unconditional cash transfers—something India is trying to do now. Yet another example comes from the Pacific island economies, which have recently expanded financial access to both small and medium enterprises and households on remote, outer islands.

Notwithstanding Asia's impressive progress in strengthening and improving its financial sector, the region's development remains unbalanced, with the financial sector still lagging the dynamic real economy. The financial systems of developing Asia remain well behind the global finance frontier. That status in and of itself is not a first-order cause for concern, but what is more relevant is that the region's financial systems do not appear to be up to the tasks of financing badly needed infrastructure investment, innovation, and extending financial inclusion to broader segments of society.

The region largely avoided the worst of the global financial crisis of 2008–09, which battered the world economy and disrupted global financial markets to an unprecedented degree. But while the worst of that crisis has abated, and growth has revived across the region, the shadow of the crisis still looms. It has given financial reform a bad name and has made more difficult the task of upgrading the financial sector to support future growth and development.

In *From Stress to Growth: Strengthening Asia's Financial Systems in a Post-Crisis World,* scholars affiliated with the Peterson Institute for International Economics, the Asian Development Bank, and other institutions around the world, address two fundamental issues. First, what are the relationships between financial sector development and economic growth, and second, what are the necessary regulatory steps needed to ensure that the financial system delivers that growth but avoids painful crises? In separate essays, the authors argue that the quality, diversity, and resilience to shocks of developing Asian financial systems must be strengthened in order to deliver crisis-free growth in coming years.

The volume examines such phenomena as the dominant role of state-owned banks, the growth of nonbank lending (the so-called shadow banks), the need to develop local capital markets, and the need for stronger supervisory institutions to ensure stability. The People's Republic of China's large financial system is discussed, with an emphasis on what lessons from the Chinese experience might be transferable to other countries around the region. Similarly, the experiences of the United States and European Union with bank stress tests are reviewed with an eye on what lessons these experiences might usefully hold for Asia. The region needs investment to improve its infrastructure and to promote technological innovation, but the book argues that the region's financial systems are inadequate in meeting those needs. Policy recommendations are made across all of these issues of concern.

We would like to express our sincere gratitude to economists from ADB, PIIE, and the other organizations who have contributed their research to this ambitious project. We would also like to give a special thanks to ADB's Donghyun Park and PIIE's Marcus Noland, who jointly managed and coordinated the project, and to ADB's Gemma B. Estrada and April Gallega and PIIE's Madona Devasahayam, Susann Luetjen, and Steven R. Weisman for facilitating the publication of the volume. I believe that this highly informative book will be a valuable resource for analysts, investors, and policymakers in Asia and beyond as a result of their and the contributing authors' efforts.

***

The Peterson Institute for International Economics is a private nonpartisan, nonprofit institution for rigorous, intellectually open, and indepth study and discussion of international economic policy. Its purpose is to identify and analyze important issues to making globalization beneficial and sustainable for the people of the United States and the world and then to develop and communicate practical new approaches for dealing with them.

The Institute's work is funded by a highly diverse group of philanthropic foundations, private corporations, and interested individuals, as well as income on its capital fund. About 35 percent of the Institute resources in our latest fiscal year were provided by contributors from outside the United States. A list of all our financial supporters for the preceding year is posted at http://www.piie.com/supporters.cfm.

The Executive Committee of the Institute's Board of Directors bears overall responsibility for the Institute's direction, gives general guidance and approval to its research program, and evaluates its performance in pursuit of its mission. The Institute's President is responsible for the identification of topics that are likely to become important over the medium term (one to three years) that should be addressed by Institute scholars. This rolling agenda is set in close consultation with the Institute's research staff, Board of Directors, and other stakeholders.

The President makes the final decision to publish any individual Institute study, following independent internal and external review of the work. Interested readers may access the data and computations underlying Institute publications for research and replication by searching titles at www.piie.com.

The Institute hopes that its research and other activities will contribute to building a stronger foundation for international economic policy around the world. We invite readers of these publications to let us know how they think we can best accomplish this objective.

The Asian Development Bank's vision is an Asia and Pacific region free of poverty. Its mission is to help its developing member countries reduce poverty and improve the quality of life of their people. Despite the region's many successes, it remains home to the majority of the world's poor. ADB is committed to reducing poverty through inclusive economic growth, environmentally sustainable growth, and regional integration.

Based in Manila, ADB is owned by 67 members, including 48 from the region. Its main instruments for helping its developing member countries are policy dialogue, loans, equity investments, guarantees, grants, and technical assistance.

Shang-Jin Wei
Chief Economist and Director General,
Economic Research and Regional
Cooperation Department
Asian Development Bank

Adam S. Posen
President
Peterson Institute for
International Economics

August 2015