OECD DEVELOPMENT CENTRE

Working Paper No. 187

(Formerly Technical Paper No. 187)

THE SOCIAL IMPACT OF GLOBALISATION IN SOUTHEAST ASIA

by

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Research programme on:
Empowering People to Meet the Challenges of Globalisation

OECD OCDE

December 2001
CD/DOC(2001)19

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ACKNOWLEDGEMENTS

The Development Centre would like to express its gratitude to the Ford Foundation for the financial support given to the project on “Income Distribution and Global Interdependence”, in the context of which this study was carried out.

PREFACE

Over the 1980s many developing countries recorded disappointing performances in terms of growth, development and, especially, poverty reduction. The 1990s has been the decade of globalisation — defined as both external opening and an increased role of markets domestically. Globalisation in developing countries has occurred largely as a consequence of moves towards external liberalisation, part of broader shift to more market-oriented, export-led development strategies, often in the framework of stabilisation and structural adjustment programmes with the IMF and World Bank. This simultaneous emphasis on globalisation with the unsatisfactory performance of developing countries in lowering inequality and poverty levels, has led to an intense debate over whether globalisation, and the development strategies associated with it, are part of the problem, or part of the solution. The debate has been largely about perceptions, rather than about well-defined propositions, in part because of lack of data, inadequate analysis, and insufficient attention paid to cultural differences.

In the light of this debate, on 30 November and1 December 2000 the Development Centre organised a policy dialogue to assess the impact of globalisation on poverty and income inequality in developing countries. What policies should developing countries pursue to achieve “inclusive globalisation”, supported by pro-poor growth? What policies should OECD member countries adopt to help them through, for example, bilateral development assistance and influencing international institutions? In the Development Centre’s tradition of frank policy dialogue between experts, policy makers and stakeholders, this particular event gave a voice to those countries and people in the world economy who do not normally participate in the meetings of international institutions.

This series of papers* consists of regional surveys of the impact of globalisation that the Centre commissioned as input and background for the dialogue. For each of three regions — Latin America, Southeast Asia and Sub-Saharan Africa, two contributions were commissioned. The first focused on the economic impact of globalisation, especially the effect on poverty and inequality. The second looked at the political economy of countries in the context of policy formulation in response to globalisation.

The results presented here and in the rest of the series show that globalisation is not the major cause of income inequality and poverty in developing countries, but has none the less contributed to the poor performance of a number of developing countries. What has differentiated winners from losers has been that globalisation has worked by amplifying the effects of pre-existing inequalities in the distribution of assets, especially human capital, and of access to infrastructure and other productive resources. In countries where inequalities were high, globalisation tended to make inequality worse; similarly globalisation has tended to increase inequalities across countries.

This analysis implies two key, development policy lessons. First, for globalisation to be pro-poor, it needs to be combined with policies which create a more equal distribution of, or access to, productive assets and resources, particularly for vulnerable groups facing the increased competition which comes with globalisation. Second, the speed and sequencing of external and domestic liberalisation must be tailored to the particular circumstances of individual countries, based on their institutional capacity to transform the economy.

Jorge Braga de Macedo
President
OECD Development Centre
5 December 2001

* *Globalisation, Poverty and Inequality in Sub-Saharan Africa: A Political Economy Appraisal*, by Yvonne M. Tsikata.

Distribution and Growth in Latin America in an Era of Structural Reform: The Impact of Globalisation, by Samuel A. Morley.

Globalisation, Liberalisation, Poverty and Income Inequality in Southeast Asia, by K.S. Jomo.

Globalisation, Growth and Income Inequality: The African Experience, by Steve Kayizzi-Mugerwa.

The Social Impact of Globalisation in Southeast Asia, by Mari Pangestu.

Where Does Inequality Come From? Ideas and Implications for Latin America, by James A. Robinson.

RÉSUMÉ

Les pays en développement doivent trouver un équilibre entre les bénéfices et les coûts de la globalisation. Si l'intensification de la concurrence peut améliorer la distribution et la productivité, les bénéfices ne se partagent de manière équitable : certains secteurs ou régions ont une croissance plus vive que d'autres. En Asie du Sud-Est, la croissance économique rapide a permis de réduire la pauvreté et les inégalités, mais ces tendances se renversent aujourd'hui. Comment faire en sorte de limiter les dégâts sociaux de la globalisation ? Nous ne savons pas encore très bien comment la globalisation influe sur la croissance, l'équité et la pauvreté, mais nous savons que la croissance joue sur l'équité et réciproquement. Réduire la pauvreté et les inégalités nécessite des conditions macro-économiques saines, une bonne gouvernance, des investissements en milieu rural afin de réduire le différentiel de croissance entre villes et campagnes, des marchés du travail flexibles, des institutions solides aptes à fournir des services sociaux et un accès généralisé à l'éducation. L'approfondissement de la démocratie permettra d'accentuer la pression en faveur de ce type de mesures, dans un contexte général d'investissements dans les infrastructures, les ressources humaines et l'environnement.

SUMMARY

Developing economies have to balance globalisation’s benefits and costs. Increased competition can lead to better distribution and productivity but benefits are not shared equally because some sectors or regions grow faster than others. In Southeast Asia, rapid economic growth has reduced inequality and poverty, but these trends have now gone into reverse. How can we ensure globalisation does minimal social damage? It is not clear how globalisation affects growth, equity and poverty, but growth affects equity and vice-versa. What is needed to reduce poverty and inequality are sound macroeconomic conditions, good governance, investment in rural areas to narrow the urban-rural growth gap, flexible labour markets, stronger institutions for provision of social services and greater access to education. More democracy will increase pressure for such measures as part of general investment in physical infrastructure, human resources and the environment.

I. INTRODUCTION

One of the biggest challenges to developing and transitional economies is how to balance the benefits of globalisation against the risks and costs. Increased competition that forces production changes in an economy will lead to better allocation of resources and greater efficiency and productivity. But net benefits are not shared equally because some groups, sectors or regions grow much faster than others. Globalisation can do good, but the jury is still out on its social impact, especially how best to manage risks and costs for the greater benefit of all.

Southeast Asia has been held up as an example of how rapid economic development can reduce income inequality and absolute poverty. But since the mid-1980s, these trends have gone into reverse, especially in recent years.

How did rapid liberalisation and globalisation in three major Southeast Asian economies — Indonesia, Malaysia and Thailand — in the 1980s and 1990s affect growth, development, inequality and distribution? The process began much later in the Philippines and had more mixed results. Different policies, institutions, initial conditions and investment in human and physical capital produced different results in all four countries. How can we ensure that globalisation, which all agree is inevitable, does minimal social damage?

II. THE SOCIAL REPORT CARD: TRENDS IN POVERTY AND INEQUALITY

Tables 1, 2 and 3 show poverty fell by two-thirds in East Asia between 1975 and 1995, the sharpest drop in any region of the world, and that life expectancy, infant mortality and access to education also improved. Indonesia, the Philippines and China achieved universal primary education and in Malaysia secondary school enrolment topped 50 per cent in 1995. Even Vietnam had 90 per cent primary school enrolment. Yet serious social problems appeared in the region before the 1997-98 economic crisis.

Note that the incidence of poverty numbers differ between Table 4 and Table 1 since the former uses nationally-defined poverty lines whereas the latter uses the $1 a day at 1985 prices measure. The broad trends are similar.

Table 1. **Poverty and Inequality Indicators in Asia**

		Share of Income or Consumption, 1987-98		Gini Coefficient				Percentage of Population below Poverty		
		Poorest 20%	Richest 20%			First Yr	Last Yr	1975	1985	1995
East Asia and Pacific				1980s-90s		38.7	38.1	57.6	37.3	21.2
Indonesia	1996	8	44.9	1970-95	E/P	34.9	34.2	64.3	32.2	11.4
Malaysia	1995	4.5	53.8	1973-95	I/P	50.1	48.5	17.4	10.8	4.3
Philippines	1997	5.4	52.3	1985-94	E/P	41	42.9	32.4	25.5	10.6
Thailand	1998	6.4	48.4	1975-92	E/P	36.4	46.2	8.1	10	<1
Vietnam	1998	8	44.5	1992-98	E/P	35.7	36.1	n.a	74	42.2
Cambodia	1997	6.9	47.6							
Lao PDR	1992	7.6	40.3	1993	E/P		30.4	n.a	61.1	41.4
China	1998	5.9	46.6	1985-95	I/P	29.9	38.8	59.5	37.9	22.2
HK China	1980	5.4	39.9	1971-91		40.9	45			
Taiwan (China)				1985-95	I/P	29	31.7			
Korea, Rep.	1993	7.5	39.3	1970-88	I/H	33.3	33.6			
Singapore				1973-89	I/H	41	39			

Notes:

1) Poverty numbers come from Table 5.1 in World Bank (1998) and are based on int. poverty line of US$1/day per person and are at 1985 prices.

2) Gini coefficients comes from the World Bank, Deininger and Squire data set on income inequality and is drawn from the data set as well as Table 5.4 in World Bank (1998). I/P is per capita income, E/P is per capita expenditure, and I/H is income per household. Whilst the Gini coefficients are not strictly comparable, the broad magnitudes and trends can still be used.

Source: World Bank (1998), and World Bank, *World Development Report,* various issues.

Table 2. **Human Development and Education Indicators**

	Life Expectancy			Infant Mortality Rate	
	1970	**1995**	**1998**	**1970**	**1995**
East Asia	**59.4**	**68.8**		**76**	**34**
Indonesia	47.9	63.7	65.6	118	51
Malaysia	61.6	71.8	72.2	45	12
Philippines	57.2	66.5	68.6	71	39
Thailand	58.4	69	68.9	73	35
Vietnam	49.36	67.5	67.8	111	42
Cambodia			53.5		
Laos	40.4	52.8	53.7	146	104
Myanmar			60.6		
China	61.7	69.4	70.1	69	34
Taiwan (China)	69	74.8		69	6
Korea, Rep.	60.6	72	72.6	46	10

Source: UNDP, *Human Development Report* and World Bank (1998).

Table 3. **Education Levels**

	Net Enrolment Ratios				% Public Expenditure	
	Primary		Secondary			
	1970	**1995**	**1970**	**1995**	**1980**	**1996**
Taiwan (China)		>99	75	87.4		
South Korea	>99	>99	45.4	93.4	3.7	3.7
Malaysia	84.1	88.7	25.5	55.9	6	5.2
Thailand	78.6	88.2	18.2	34.9	3.4	4.1
Indonesia	75.6	>99	13	55	1.7	1.4
China	75.9	>99	34.7	50.7	2.5	2.3
Philippines	>99	>99	40.4	75.5	1.7	2.2
Myanmar	30.8	70	3.7	13.3	1.7	1.2
Lao PDR	n.a.	60	n.a	15	..	2.5
Vietnam	n.a.	91	n.a	45	..	2.6

Source: World Bank, *World Development Report.*

Table 4. **Changes in Poverty Profile**

	Indonesia				**Thailand**			
	Urban	**Rural**	**Total**		**Urban**	**Rural**	**Total**	
1976	38.8	40.4	40.1	1962/3*	38.0	61.0	57.0	
1980	29.0	28.4	28.6	1968/98*	25.0	45.0	42.0	
1987	20.1	16.1	17.4	1975/6*	22.0	37.0	33.0	
1990	16.8	14.3	15.1	1980/81*	21.0	35.0	31.0	
1993	13.4	13.8	13.7	1975/6	n.a	n.a	30.0	
1996	9.7	12.3	11.3	1981	n.a	n.a	23	
1998	21.9	25.7	24.2	1986	n.a	n.a	29.5	
1999	na	na	20.3	1988	n.a	n.a	22.8	
				1990	11.9	22.9	20.1	
				1992	7.6	16.9	14.5	
				1994	7.2	13.1	11.5	
				1996	4.0	7.2	6.4	
				1998	3.9	7.0	6.1	
	Malaysia				**Malaysia**			
	Urban	**Rural**	**Total**		**Malay**	**Chinese**	**Indian**	**Others**
1970	21.9	58.7	49.3	1970	64.8	26.0	39.2	44.8
1976	17.9	47.8	39.6	1976	56.4	19.2	28.5	44.6
1984	8.2	24.7	18.4	1984	25.8	7.8	10.1	22.0
1987	7.3	19.3	15.0	1987	23.8	7.1	9.7	24.3
1995	3.7	15.3	8.9	1990	20.8	5.7	8.0	18.0
1997	2.1	10.9	6.1					
1998	1.9	10.0	5.5					
	Philippines				**Korea**			
		Rural	**Total**		**Urban**	**Rural**	**Total**	
1985	45.0	53.1	40.9	1980	26.2	21.3	24.5	
1988		45.7	34.4	1985	13.5	7.2	11.0	
1991		48.6	34.3	1988	8.9	7.2	8.4	
1994	29.0	45.4	32.1	1993	8.8	9.3	8.2	
1997		36.9	25.0	1996	6.1	9.4	7.0	

Notes:
* Thai series based on household consumption function methodology, rest of Thai data based on nutritional adequacy method, series III for 1990-98, series II for 1988 and series I from 1975/6-86 (from Tables 1 and 2 in Phongpaichit and Sarntisart, 2000).
Source: Indonesia: Central Bureau of Statistics; Thailand: taken from various tables in Phonpaichit and Sarntisart which draws the data from Thai Household Socio-economic Survey; Malaysia taken from bin Yusoff *et al.* and comes from various issues of Government of Malaysia, Malaysia Plan; Philippines comes from World Bank, Philippines: Growth with Equity, the Remaining Agenda, 2000.

The definition of poverty proved inadequate. For example, the number of "near poor", just above the poverty line, remains large. Poverty also depends on urban-rural, regional, gender and ethnic differences. The crisis underlined too that poor or vulnerable people have no social safety nets.

Less absolute poverty does not always mean more equity. East Asia is said to have achieved "growth with equity", but this is not always borne out by the data (World Bank, 1998). Average Gini coefficients show income/expenditure distribution in East Asia has not changed in the last 15 years and that distribution is more equal than in Latin America.

Table 5. **Changes in Inequality in Asia**

Thailand*		**Indonesia**				**Malaysia**			
			Urban	Rural	Total		Urban	Rural	Total
1962	45.6								
1968	48.2	1976	35	31	34	1970	50.5	46.9	51.3
1971	53.5	1978	38	34	38	1976	51.2	50.0	52.9
1975	42.6	1980	36	31	34	1979	50.0	48.2	50.8
1980	45.3	1981	33	29	33	1984	46.6	44.0	48.0
1985	50.0	1984	32	28	33	1987	44.9	42.7	45.6
1988	49.3	1987	32	26	32	1989	44.5	40.9	44.5
1990	51.3	1990	34	25	32	1990			44.6
1992	53.1	1993	33	26	34	1995			46.2
1994	51.8	1996	36	27	36	1997			47.0
1996	51.1	1997	na	na	38	1998			46.8
1998	50.8	1998	na	na	37				
1999	53.0								

Philippines		**Korea, Rep.**				**China**		**Hong Kong**		**Taiwan**	
			Urban	Rural	Total						
		1970	34.55	29.45	33.2	1980	32.0	1971	40.9	1970	29.4
1971	49.4	1971			36.0	1982	28.2	1973	39.8	1973	33.6
1985	46.1	1976	41.18	32.73	39.1	1983	27.2	1976	40.9	1978	28.4
1988	45.7	1980	40.5	35.55	38.9	1984	25.7	1980	37.3	1980	28.0
1991	45.0	1982	37.05	30.61	35.7	1985	31.4	1981	45.2	1985	29.2
1994	42.9	1985	36.94	26.69	34.5	1986	33.3	1986	42.0	1988	30.0
1997	46.2	1988	34.96	28.95	33.6	1987	34.4	1991	45.0	1990	30.1
		1990	32.39	29.91	32.26	1988	34.9			1991	30.5
		1993	30.63	31.01	31.0	1989	36.0			1992	30.8
		1996	28.9	30.88	29.54	1990	34.6			1993	30.8
						1991	36.2				
						1992	37.8				
						1995	41.5				
						1998	40.3				

Source: Thailand, Series I (1962-71), Series II (1975-88), Series III (1990-8) see Table 3 from Pongphaichit and Sarntisart (2000); Indonesia from Table 3.3 in Feridhanusetyawan (2000) and drawn from Central Bureau of Statistics, Booth (2000) and World Bank (2000*b*); Malaysia from Table. 6 in Zin (1999) and 1990-97 as quoted in Yusuf (1999); Philippines from World Bank, Deinenger and Squire Inequality data set and WDR; China from Ying (1995, and taken from Deinenger and Squire data) and 1998 from WDR; Korea, HK and Taiwan from Deininger and Squire data set, and for recent Korean numbers from Moon (1999).

In Southeast Asia (except Thailand), distribution inequality changed little or fell until the early 1990s before rising in the last part of the decade. The opposite happened in Thailand. Inequality has steadily risen in China since the 1970s before falling slightly in 1998. In Korea, it seems to have fallen up to 1993. These trends also mask inequalities based on ethnicity, region, urban-rural differences and gender, which have been more important since the crisis and a source of tension in some countries.

First Phase of Development and Liberalisation (1970 to mid-1980s)

The four Southeast Asian economies were agriculture-based exporters of raw materials until the 1970s. All of them industrialised by import substitution (IS) and then switched to exporting, mainly of unskilled labour-intensive goods that tend to be "pro poor" by employing many people with only primary education. Often import substitution continued.

Absolute Poverty, Inequality and Growth

The four economies contained great poverty and inequality when they began industrialising in the early 1970s. During the 1970s and into the 1980s, their growth was quite high (above 5 per cent). In the Philippines it was more uneven — 6 per cent in the 1970s, falling to 1 per cent in the 1980s. Despite similar growth rates, poverty and distribution inequality trends differed.

The effect on poverty was dramatic. All the countries except the Philippines saw a sharp fall in poverty in the first half of the 1970s. In Malaysia and Indonesia, distribution inequality increased at first. The Philippines economy grew about 6 per cent for most of the 1970s due to IS and industrialisation, but poverty and distribution inequality changed little.

The pattern altered between the mid-1970s and the mid-1980s. Poverty continued to fall in Indonesia and Malaysia, but rose again in Thailand in the mid-1980s. The changes were mainly due to the price of farm products. The Gini inequity coefficient declined steadily for Malaysia and Indonesia. In Thailand, it rose for the entire period because of a widening gap between rural and urban households. The Philippines saw little change in poverty or distribution, so poverty there was double that of the rest of the region in 1985.

In this mixed pattern of growth, poverty and inequity, Indonesia and Malaysia were more typical, with inequality increasing and then decreasing with economic growth. Thailand shows the opposite, with inequality rising for most of the period. Growth caused this, but decline in income inequality led to more growth in Malaysia and Indonesia.

Poverty can be reduced either by economic growth that boosts income or by improving distribution. Table 6 shows that the fall in poverty in Malaysia and Indonesia for much of the period was mainly due to growth rather than inequality changes. Growth was the main cause of less poverty, but less inequality also helped reduce it in Malaysia for the whole period and in Indonesia between 1978 and 1984. Policies that improved distribution, such as the New Economic Policy (NEP) and rural development in Malaysia, helped reduce poverty. But greater inequality cancelled out growth-driven poverty reduction and made people even poorer in Thailand.

Table 6. **Measures of Inequality in East Asia**

	Fall in Poverty Rates	Change in Poverty due to Growth	Change in Poverty due to Changes in Inequality	Residual
Malaysia				
1973-89	19.1	16.4	3.9	-1.2
Thailand				
1975-86	-1.9	6.1	-11.0	3.0
1986-92	10.0	10.0	-1.5	1.5
Philippines				
1985-88	5.0	5.2	-0.3	0.1
1988-91	-1.2	2.9	-4.1	0.0
1991-94	1.7	0.8	1.0	-0.1
Indonesia				
1970-78	3.8	7.6	-2.7	-1.1
1978-84	26.7	18.5	3.4	4.8
1985-95	23.6	22.4	-3.1	4.3
China (rural)				
1985-90				

Note: a positive figure is a reduction in the poverty rate; a negative figure is an increase.
Source: Taken from Table 1, Indonesia and Poverty (sector background, Social Policy and Governance, www.worldbank.org).

Urban-rural, regional and ethnic factors help explain poverty and inequality changes.

The Rural-urban Factor

Two-thirds of the region's poor still live in the countryside. The urban poor have increased due to emigration to the towns. Rural poverty was greater than urban in all the countries in the early 1970s, with the biggest disparity (three to one) in Malaysia. In the Philippines and Thailand, rural poverty was double that in the towns, while in Indonesia it was only slightly greater. The main reason seems to be initial conditions.

In the 1970s, urban and rural poverty declined at different rates, though between 1970 and 1976, they fell in tandem in Malaysia. During Indonesia's oil boom, poverty dropped much faster in towns than in the countryside because construction and IS activity was mainly in the towns. In the late 1970s, the trend changed and rural poverty declined more quickly than in urban areas. By 1980, rural poverty was slightly lower than urban and by 1987 much lower. This was probably due to the government spending oil revenues on rural infrastructure and rice self-sufficiency, which boosted the farm sector.

In Thailand, poverty declined faster in towns than in the countryside, especially in the Bangkok area because of industrialisation (Phongpaichit and Sarntisart, 2000), but rural poverty was still about double the urban rate.

Urban-rural and regional inequality differences are significant in each country. In Indonesia and Malaysia, urban and rural inequity grew until the mid-1970s then declined as both countries boosted rural development. However, urban inequality was still higher by the mid-1980s, especially in Indonesia. Urban inequity was higher probably because wages in the modern formal sector rose much quicker than in the informal sector and growth only benefited a few groups.

Regional Dimensions

Poverty and inequality vary inside each country. Urban inequality in Indonesia is greater in towns in Java than in towns elsewhere. Worsening expenditure distribution in urban areas went hand-in-hand with deeper urban poverty during the period, so the oil boom probably benefited more the capital-intensive sectors in towns in Java (Booth, 2000).

Poverty was lowest in Peninsular Malaysia and highest in Sabah (three times as high), followed by Sarawak (twice as high). Poverty in Sabah increased with an influx of illegal immigrants and perhaps because the government cut spending in the late 1980s and mid 1990s (Zin, 2000:125).

The most equal income distribution was in Johor with a Gini coefficient of 38.6 and the highest in the East Malaysian states of Sabah (45.9) and Sarawak (44.8). The rich states of Selangor and Terengganu were also high, due to an influx of workers from other states in search of better-paying jobs (bin Yusoff *et al.*, 2000).

Regional disparity in Thailand, especially between the Bangkok and central district and the poor north east, is very high (Table 4B). In GDP growth, share of GDP, poverty level and average per capita income, the central and Bangkok area was very much better off than other regions. The north east was worst off due to scant resources, low rainfall, poor soil and lack of investment in physical (irrigation) and human (education) capital.

Ethnic Disparities

Ethnic disparities in poverty were sharpest in Malaysia and created the most tension because of a more equal balance of ethnic groups there. Most country people were Malay farmers, while the Chinese lived mainly in towns and worked in industry or commerce. In 1970, 65 per cent of Malays were poor, compared with 26 per cent of Chinese. Malays were poor because of low pay in the countryside, especially in farming. Education was the key factor in poverty in Malaysia until the mid-1970s (bin Yusoff *et al.*, 2000). Poorer education among Malays barred them from better-paid industrial sector jobs.

There were major ethnic disparities in income and asset distribution too. Malays earned half as much as Chinese in 1970. Tensions between them led to riots in May 1969 and the government shifted to “growth with equity” and in 1971 to the NEP, which aimed at equity between ethnic groups.

Economic growth plus policies such as the NEP reduced the high poverty rate among Malaysians, including the large number who were Malays (Bumiputeras). This decline was dramatic for all ethnic groups, though slightly lower for the Bumiputeras perhaps because of education levels and more Bumiputeras being country-dwellers. Income disparities between ethnic groups also remained. The mean per capita income (in real terms) of Malays grew slightly more than that of the Chinese (140 versus 110 per cent) between 1970 and 1984 and the gap between them narrowed from 100 per cent to 75 per cent (bin Yusoff *et al.*, 2000).

Ethnic groups in the other countries are not as equally balanced as in Malaysia. Many people feel the Chinese have an undue share in Southeast Asian economies. They tend to live in towns and work in commerce. This has always been a source of tension in Indonesia.

Rapid Liberalisation and Opening-up

Rapid globalisation occurred between the mid-1980s and the mid-1990s when all Southeast Asian economies aggressively exported goods and were shifting away from labour-intensive items to those requiring more skilled labour. They had liberalised the financial sector and attracted much foreign capital.

Absolute Poverty, Inequality and Growth

Absolute poverty continued to fall in Indonesia and Malaysia, as well as now in Thailand and the Philippines. By 1996, a year before the crisis, poverty was below 10 per cent in Malaysia and Thailand and just above that in Indonesia. In the Philippines, it had declined from 41 to 34 per cent by 1991 and then fell dramatically to 25 per cent by 1997, though this was still more than double that of its ASEAN neighbours.

Growth in the Philippines was still much lower than elsewhere in Southeast Asia, averaging 3.3 per cent between 1990 and 1998, with per capita income growth of only 0.8 per cent. It was striking that poverty declined rapidly during this period despite the slower growth.

The dramatic fall in poverty figures hides important problems, notably that of the near-poor. In Indonesia, raising the poverty line by 25 per cent more than doubled the percentage of people below it from 11 to 25 per cent in 1996. Many areas outside Java were in a poverty trap with high levels of absolute poverty.

Trends in inequality were also reversed during the period. It declined in Thailand and increased in Malaysia and Indonesia in the 1990s. In the Philippines, it fell between 1984 and 1994, though there were fluctuations that affected the poverty rate. Between 1985 and 1988, growth reduced poverty substantially and more than offset the increase caused by more inequitable distribution. But in 1988-91, worsening income distribution cancelled out the positive effect of growth. In 1991-94, both factors helped reduce poverty, but distribution inequality grew again in 1994-97.

Income inequality in Thailand grew until 1992, except for 1988 (due to very high crop prices). Then the Gini coefficient declined (1992-96), as did the per capita income gap between Bangkok and the north eastern region. The income distribution improvement was probably due to a tight labour market that produced higher real wages in the formal and manufacturing sectors. Unequal access and insufficient investment in secondary education are still the main causes of inequity. The fruits of government emphasis on secondary education in the 1990s have not yet reached the labour market.

Rural-urban Dimensions

Trends in urban-rural poverty also changed significantly. In Indonesia and Malaysia, urban poverty fell much faster than rural, meaning towns probably benefited more from the rapid globalisation. In Indonesia, this shrank urban poverty to below the rural poverty rate, contrary to the situation in much of the 1970s until the late 1980s. In Malaysia, rural poverty is now five times higher than urban, up from three times higher in the previous period. But poverty in Thailand fell slightly faster in rural than urban areas, probably because rural workers were absorbed by the fast-growing urban sector and sending remittances back to the countryside. Wages and remittances were about a quarter of all rural incomes, and higher among poorer people (Phongpaichit and Sarntisart, 2000)[1]. Two-thirds of all poverty in the Philippines is rural and more than half the poor have only primary education or less.

Both urban and rural inequality rose in Indonesia right up until the 1997 crisis, matching the worsening relative poverty. Overall national inequities were affected by urban-rural inequalities rather than inter-provincial ones and education was a key factor (Akita *et al.*, 1999).

In Malaysia, the rural-urban income gap widened during the 1990s. Interracial income disparity increased too, with the Chinese mean monthly household income growing faster than that of the Bumiputeras, boosting the disparity ratio from 1:1.80 in 1995 to 1:1.83 in 1997 (Yusuf, 1999).

The worsening effect of the boom period on distribution is also shown by increased relative poverty in both urban and rural Indonesia. From 1987 to 1996, relative poverty (the number of people spending less than 50 per cent of their income) increased from 17 to 21 per cent (Feridhanusetyawan, 2000). Poverty also varied widely from region to region, with some extremes — in 1990 the figure was 13 per cent in Jakarta and 46 per cent in East Nusa Tenggara (World Bank, 2000).

Regional and Gender Dimensions

Geographical differences partly explain the rise in inequity in Malaysia. Half of all poor households are in Terengganu, Kelantan and Sabah, mainly in the north east. In Thailand, poverty fell much faster in the Bangkok area, which has the country's lowest poverty rate — less than half a per cent by 1996. The north east has the highest (10 per cent) and also the most poor people.

Regional inequality is acute in Thailand, and differences in poverty rates, income growth and per capita income are increasing. The gap between the highest per capita region (Bangkok) and the lowest (the north east) increased from about seven times in 1982 to nine times in 1992.

Women in Malaysia seem to have benefited equally from rapid economic growth, with little difference in poverty between female and male-headed households. But there has been scant increase in the proportion of female labour, which only grew from 46.6 to 47.1 per cent between 1970 and 1995. Women's wages were only half those of men in 1987-91, which suggests wage discrimination rather than different education levels.

The 1997 Economic Crisis

The impact on the poor of the crisis that began in 1997 and led to contraction in 1998 of all the economies studied here was compounded by drought in 1997 and heavy rains in 1998, bringing crop failures as well as forest fires in Indonesia. The economic crisis was aggravated by a political crisis in some countries, especially Indonesia. The political crisis heightened social tensions caused partly by income and wealth disparities.

The economic crisis worsened poverty and inequality, but the social impact was less than predicted (World Bank, 2000*a*), though some effects, such as the drop in spending on health and family planning, will only be felt later. The fall in output did not last long and labour migration from the worst-hit cities to the countryside softened the impact in urban areas. Instead of spending less, people drew on their savings and cut out non-essential items. And government work and safety-net programmes helped reduce the social impact (World Bank, 2000*a*:116), though it was still significant and reversed the dramatic trend of declining poverty.

Poverty increased in Thailand and Indonesia but not in the Philippines and Malaysia. Consistent estimates of absolute poverty show that Indonesians living below the poverty line increased from 11 to 20 per cent between 1996 and 1998 — around 20 million people — and then declined slightly to 19 per cent in 1999 (Feridhanusetyawan, 2000). This sets Indonesia back to its 1990 poverty level. In Thailand, poverty rose only slightly, affecting the rural not the urban poor. The largest rise in poverty was in the south and central regions followed by the north east.

The workforce in Indonesia and Thailand was mostly hit by falling real wages and under-employment, rather than open unemployment, which rose only slightly in the four economies (World Bank, 1998). Younger, less-educated and informal sector workers were the most affected. Indonesia was the only crisis country with high inflation and so felt the greatest impact on real wages, which fell by 34 per cent in the formal sector and 40 per cent in agriculture. Jobs also shifted from the formal to the informal sector and from the modern to the agriculture sector, depressing wages.

In Thailand, real income dropped most for people with less than primary education (World Bank, 1998). As in Indonesia, the main effect has been the decline in real wages — by 20-25 per cent between first quarter 1998 and third quarter 1999, when a third of all workers earned less than the minimum wage (162 baht in Bangkok and 130 baht elsewhere). Despite the government programme, only 10-13 per cent of the unemployed got severance pay. (Phongpaichit and Sarntisart, 2000).

In the Philippines, open unemployment increased by one million in 1997-98, raising the jobless rate to 13.3 per cent, mostly in the farm sector because of drought and affecting unpaid family workers and independent farmers most. Being a net exporter of labour helped in the crisis. Real wages were largely unchanged.

In Malaysia, open unemployment rose slightly, but foreign workers (a fifth of the labour force, mostly Indonesians) accounted for most of the job losses and increased under-employment. Workers in Indonesia and Thailand returned to their villages, thus limiting the rise in urban poverty, and also switched from the formal sector to self-employment, unpaid family work and farming.

The effect of the crisis on women workers has been mixed. Their number fell in Korea and Malaysia, was unchanged in Thailand and even increased in Indonesia, where they took jobs to make up for the large income drop (World Bank, 2000*a*).

Inequity was mostly unchanged, although it declined slightly in Indonesia and increased a little in Thailand. In Indonesia, the rich cut back expenditure during the crisis more than the poor, who drew on their savings, so household consumption fell by only by 3 per cent, compared with the overall 1998 economic contraction of 14 per cent. The crisis hit Jakarta and cities in West Java most, while some off-Java areas had an export boom from increased farm exports, such as cloves, because of higher prices as well as the sizeable depreciation of the rupiah. The relative change in food prices due to currency devaluation hurt the urban poor and rural workers who are net consumers, but benefited the rural poor who are net producers.

In Thailand, the Gini coefficient may have increased to 53 in 1999, reversing the earlier decline (Phongpaichit and Sarntisart, 2000). The rise in inequity was due to a bigger wage gap between skilled and unskilled workers and higher income increases in the Bangkok area than elsewhere. Rural poverty rose despite the bigger impact on urban areas. The drop in real income most affected those with less than primary education.

It was feared that government cuts in basic social services spending and reduced household expenditure on health and education would have severe consequences. But effects have been mixed, as health care spending and school enrolment did not decline as sharply as expected. However the drop in enrolment among the poor is worrying as it widens the education gap between rich and poor that causes inequality.

The crisis reversed the trend towards greater (and formal wage) employment in towns. Whether it will pick up again at the rates of the 1990s will depend on the extent of economic recovery, which in some countries is still small.

III. THE EXPERIENCE WITH GLOBALISATION

We now look at the trade, investment and capital account policies in Southeast Asian economies aimed at integrating them with the world economy.

First Phase of Opening Up

The four Southeast Asian economies were resource-rich and agrarian-based, relying on a few primary commodities and agricultural exports to earn foreign exchange. All had an IS policy until the mid-1980s because they wanted to create a modern domestic industrial sector to produce first consumer goods and then intermediate and capital goods. All used tariffs on finished goods, which were then gradually applied to intermediate and capital goods. Non-tariff barriers were increasingly used.

The result was a complex protection structure biased against exports and agriculture and producing manufactured goods inefficiently and expensively. IS industries also tended to be concentrated in towns and in capital-intensive production with less benefit to labour. So reduction of poverty and inequality was more due to policies of improving infrastructure and agriculture.

At the same time, all four countries began encouraging export orientation (EO) because IS was limited by a small domestic market as well as external developments that stressed the need to earn foreign exchange. EO first emphasised unskilled labour-intensive manufactured exports (because they had comparative advantage), largely to offset the bias against exports created by the IS-caused protection system. So instruments were introduced such as duty drawbacks or exemptions for imported inputs, export processing zones and export subsidies and credit, along with investment incentives.

From the 1970s until the mid-1980s, Thai development strategy centred on agriculture and IS industrialisation, with EO introduced in 1971. Dependence on imported inputs for IS and a deteriorating balance of payments also encouraged incorporation of EO into industrialisation strategy. Exports were prioritised without changing the protection structure. The government found it hard to change tariffs because it depended on these revenues. Export promotion through tax breaks was largely ineffective as the EO sector was still held back by the anti-export IS sectors. The IS-EO conflict was not resolved until the mid-1980s. The annual growth rate was an impressive 8.5 per cent but most exports were still raw materials, especially rice, rubber, tin and maize. By 1980, nearly half of all exports were still agricultural and only 22 per cent were manufactured goods, mainly resource-based.

Things went wrong for Thailand in the early 1980s. Prices of its main farm exports fell, oil prices rose and agricultural expansion slowed for want of new land. The need to finance growth because of limited foreign exchange from exports had incurred a large foreign debt, which the government tackled with fiscal consolidation, devaluation of the baht and moves towards liberalising trade and investment. Growth was held at 5 per cent between 1980 and 1986 and manufactured exports began to rise, though in 1985 farm products were still 40 per cent of all exports and labour-intensive exports about 18 per cent.

Malaysia adopted a moderate IS policy much earlier than the other Southeast Asian countries. Most of its IS industries were on the edge of major towns in West Malaysia or near the final market. By 1970, it had adopted EO industrialisation alongside its IS strategy. IS industries were producing inefficiently behind high tariff and non-tariff barriers, with little linkage to other domestic industries. Riots in 1969 and serious regional and ethnic imbalances in the country's development, as well as the mid-1970s recession, spurred a rethink of industrialisation strategy.

The first focus of Malaysia's EO drive was labour-intensive industries such as textiles, garments and electronics (especially assembling and packaging semiconductors) with the aim of attracting foreign investors, who got subsidised export credit, tax breaks, export-related subsidies, investment incentives and duty free imports. The government created industrial estates and free trade zones and many foreign firms set up in export-processing zones such as Penang. Over the last 20 years, local supplier industries have grown up alongside the transnational companies.

Until the early 1980s, Indonesia had an inward-looking IS industrialisation approach, with the government playing a key role either through state-owned firms in heavy industries such as oil refining, cement, aircraft, steel and fertilisers, or through regulations. The Indonesian economy grew during the 1970s and early 1980s because of IS industrialisation from final goods and then intermediate and capital goods and more processing of resource-based industries such as plywood. Growth was induced by direct government spending on infrastructure and a drive for rice self sufficiency dating from the early 1970s.

Indonesia started deregulating and liberalising after the first drop in oil prices in the early 1980s. Steps included devaluation of the rupiah, fiscal consolidation, postponement of large government projects, liberalisation of interest rates for state banks and measures to attract foreign investment in EO industries. However, liberalisation was ambivalent because the government tackled the worsening balance of payments by curbing imports with a very protectionist import licensing scheme and creating a ministry for utilisation of domestic products.

In the Philippines, IS-led growth accumulated capital but also inefficiency, so was sluggish.

All four economies had sound macroeconomic policies and kept inflation under control, except for the Philippines. For most of the 1970s and into the 1980s, exchange rates were linked to the US dollar either by a fixed exchange rate or managed float system. Devaluations coped with current account deficits and helped boost exports: Indonesia devalued the rupiah twice when oil prices fell and the current account deficit rose and Thailand devalued the baht. The aim was to help diversify exports away from oil and primary commodities. Southeast Asian governments also cut budgets and tried to raise tax revenue.

They all continued to develop their agricultural sector in different ways. Indonesia used its oil revenue windfall to provide basic social services, rural infrastructure and agriculture. The rice self-sufficiency program was part of this policy and government investment and technological advances in rice varieties steadily boosted food production. Increased productivity meant farm jobs grew slower than jobs in the whole economy. Employment grew quickly in the booming non-agricultural sectors of government construction, services and IS industries in urban areas.

Government infrastructural investment focused in and around Bangkok, where virtually all manufacturing is. The overall tax on rice exports depressed rice prices and urban industrial labour costs (Dixon:87). The government also invested in physical infrastructure — linking rural and urban areas as well as the periphery with the centre — and in universal primary education and basic health services, notably family planning.

Rapid Globalisation: Second Phase of Export Orientation and Capital Inflows

Reason for Policy Shift

The more aggressive switch to EO in the four economies came in the mid-1980s. They were able to keep up IS policies much longer than Northeast Asian economies, such as Korea and China (Taipeh), because they could earn foreign exchange from exporting raw materials, though reliance on a narrow range of these made them vulnerable to changes in demand and price. Korea and China (Taipeh) had few natural resources so EO of manufactured goods was logical for growth (Masuyama *et al.*, 1997:8). The major industrialisation shift to EO in manufactured goods in Southeast Asia therefore did not happen until the price of their commodity exports collapsed in the mid-1980s. World-wide recession also preceded the 1986 fall in oil prices and the need to diversify exports became imperative.

Thai policymakers and business people also saw the political changes in Indochina as a chance to develop Thailand as a regional centre, especially in finance. The greater global capital flows of the 1990s and continued high cost of funds from the inefficient domestic banking sector also made it attractive to tap funds from global capital markets (Phongpaichit and Sarntisart, 2000).

The mid-1980s recession affected Malaysia too. Its economy contracted by 1 per cent in 1985, foreign direct investment fell sharply and there was a banking crisis.

The macroeconomic trade and foreign investment policy shift aimed to boost exports and efficiency of resource allocation in line with comparative advantage. The Southeast Asia industrialisation model, as in Korea and China (Taipeh), emphasised education.

But unlike Korea and China (Taipeh), which at the same level of development used export promotion policies such as subsidies and targeting sectors, the Southeast Asian economies from the mid-1980s deregulated and liberalised trade barriers and investment restrictions more broadly (Bora *et al.*). This more liberal market-oriented policy to promote EO was due to a shift towards a "neutral" policy environment rather than favouring exports or imports, to greater trade friction with major partners (the US and EU) and to changes in the rules.

The rules and commitments of the GATT — and since 1995 the WTO — affected the policies these countries could pursue. Export subsidies were no longer available to those signing on to the GATT Subsidies and Countervailing Duties Code. Rapid export growth in these countries in the early 1980s led major importers such as the US to press them to sign the Code and so eliminate export subsidies. The 1992 ASEAN Free Trade Area (AFTA) which sought to reduce tariffs on all goods to 0-5 per cent for intra ASEAN trade, and the APEC agreement, also had a big influence on tariff reduction and deregulation by these countries. When Indonesia hosted APEC in 1994, it launched a tariff reduction program and eliminated many curbs on foreign investment. When the Philippines hosted the APEC meeting in 1996, it too announced tariff reductions and investment liberalisation.

Southeast Asia was more open to foreign investment and personnel, skilled and semi-skilled. Malaysia has depended on foreigners to make up for its labour shortage. The region also developed a much more market-oriented financial system, so financing through capital markets and other private sources helped fund export manufacturing as well as needed infrastructure.

Macroeconomic Policy Adjustments

The main macroeconomic policy adjustments were devaluation and fiscal consolidation, often combined with monetary policy adjustments. Inflation was kept stable. Indonesia devalued its rupiah by 50 per cent and adopted a floating exchange rate around a predictable band. Macro-adjustment to offset overheating from capital inflows in the 1990s and inflation was done mainly through monetary policy (which led to high domestic interest rates and encouraged offshore borrowing), budgetary cuts and consolidation in the form of smaller subsidies for state enterprises and postponement of big government projects.

Trade Liberalisation

Trade policy aimed chiefly at removing protection in stages, first changing non-tariff barriers to tariff equivalents and then rationalising and reducing them. Exports were also encouraged by streamlining customs procedures and removing other bureaucratic bottlenecks, eliminating extra costs for exporters who have to import their inputs. So EO industries continued alongside IS ones as trade barriers started to come down. Malaysia also began an aggressive second round of import substitution by developing heavy industries such as vehicles, cement and steel.

Indonesia adopted all those policies, including the controversial replacement of the corrupt customs system with the foreign surveyor SGS. Protection was still relatively high but EO was encouraged by duty-free imports for exports and export-processing zones.

Foreign Investment Policy

All the countries competed for foreign investment thought to be important for export market access and know-how for EO industries. Foreign investment deregulation was linked to EO, so removal of restrictions or provision of incentives was linked to investments exporting a certain amount of their production. Deregulation included allowing almost full foreign ownership in EO investments. Malaysia also introduced fiscal and other incentives for research and development (R&D). In Thailand, investment privileges were linked to export activity and siting of industries in the provinces. All the economies conditioned the best incentives and the least ownership and operational restrictions on the degree of EO.

Capital and Financial Sector

All the countries began to liberalise the financial sector and capital account in quite different ways. Indonesia had had an open capital account since 1969, with few controls or reporting requirements, and also went furthest in opening up its financial sector in the late 1980s. Continued restrictions on the Thai banking sector spawned non-bank financial institutions which were the main conduit of capital inflows. But in Thailand and Indonesia, these inflows were channelled through unsound institutions and while the money fuelled growth, there was gross over-investment in non-traded goods, especially property and infrastructure, as well as over-capacity. Malaysia's problem was expansion of domestic credit. The Philippines had just started to receive capital inflows and, thanks to a banking crisis in the 1980s, had sturdier institutions.

Outcomes

Growth and structural change. Speedy globalisation led to rapid growth of GDP and exports and these economies became more part of the world economy. There were also major structural changes in GDPs and in Indonesia, the share of the manufacturing overtook agriculture for the first time in 1990.

Growth had been rapid, but exports peaked in first quarter 1995 for the four Southeast Asian economies and Korea and the subsequent drop was sharp and unprecedented (World Bank, 1998:20). Export growth for the nine East Asian economies declined from 19 and 21 per cent in 1994 and 1995 to only 4 per cent in 1996. Thailand’s exports contracted by 1 per cent, and exports by Korea, China, Hong Kong, China (Taipeh) and Singapore increased by less than 5 per cent. Malaysia’s exports grew just 6 per cent and only Indonesia and the Philippines had reasonable growth of 9 and 14 per cent. Indonesia was helped by the price of oil. Two-thirds of the slowdown appears due to cyclical factors such as the big drop in world trade growth, Japanese yen depreciation which boosted competition, real effective exchange rate appreciation due to large capital inflows, and significant drops in major export prices. Structural factors included increased competition with China and trade diversion due to NAFTA (World Bank, 2000).

Change in export composition. Apart from rapid growth, East Asian exports are also changing dramatically from resource and unskilled labour-intensive items to more skill- and capital- intensive ones. In 1990, most of the countries were still dependent on the old resource-based exports — 40 per cent of total exports in Thailand, 54 per cent in Malaysia and as much as 72 per cent in Indonesia. By comparison, 40 per cent of China’s exports were resource-based. A third of exports by Singapore and Malaysia were high-tech, mainly electronics. By 1995, Singapore and Malaysia had doubled the share of high-tech products in their exports, while in Thailand it almost tripled. In 1995, the share of electronics in total exports rose from 30 to 50 per cent in Malaysia, from 25 to 45 per cent in the Philippines, from less than 20 to 35 per cent in Thailand, from 25 to nearly 40 per cent in Korea and from slightly more than 10 per cent to close to 20 per cent in China. Indonesia reduced its share of resource-based exports, but increased that of low technology or unskilled labour intensive ones. It was only just getting into electronic exports and by 1995 their share of total exports was only about 5 per cent.

In Thailand, agriculture's share of total exports fell to only 11 per cent by 1995. At first, the main manufactured export category was unskilled labour-intensive goods (textiles, toys and wood products) which by 1990 accounted for 30 per cent of total exports. However from the late 1980s, the fastest growing exports were technology-based manufactures (especially automobiles and parts, electronics, and electrical goods) thanks mainly to Japanese investors setting up production and regional centres in Thailand. By the late 1990s, this category accounted for almost half of all exports and the share of labour-intensive and resource-based manufactures had declined (Phaipongchit and Sarntisart, 2000).

The share of non-oil items in Indonesia's total exports doubled to 60 per cent. Manufactured exports were first labour-intensive products (garments and footwear) and from resource-intensive sectors (wood and paper), but just before the crisis broke a shift to technology and human capital intensive exports (electronics) was starting. Again, relocation of investments by Japan and Korea was a big factor.

The speedy integration of East Asia with the world economy trade and investment-wise was accelerated by the “coincidence” of push and pull factors. In the mid-1980s, these economies' efforts to accelerate their EO drive and so become more attractive sites (the pull factor) for production and export bases coincided with the outward investment drive of firms in Japan and the newly-industrialised East Asian economies of Korea and China (Taipeh). Costs were rising for these firms because of the appreciation of their currencies, rising wages, labour shortages and graduation from privileges under the General System of Preferences (GSP). The investments were mainly intended as export bases, although most aimed eventually to sell to the domestic market too. The globalisation of production, with the process divided up into components and stages, was also behind this pattern. What may also have spurred the more rapid shift from unskilled labour-intensive exports in Southeast Asia was competition from low-cost producers such as China, and increasingly Vietnam and some of the South Asian economies.

So EO from the mid-1980s to the 1990s meant a speedier shift away from unskilled labour-intensive exports, and into specialisation, large shares of high-tech exports and — because of the trade-investment links — subcontracting relationships and numerous links within East Asia. Export structures became less diversified and more interdependent and exposed these countries to greater risks of trade decline and excess capacity, as in 1996, as well as contagion.

The East Asian economies expanded capacity and captured significant market share in electronics in different ways. Easy money enabled Korea and Thailand to set up domestic firms. Korea's strategy was more risky as it involved big investments and was part of the national industrial development strategy. In Thailand, the domestic firms set up were targeted as independent second-tier suppliers and subcontractors to multinational firms. Malaysia, the Philippines, and to a lesser extent Indonesia, were safer as part of the production network of multinational companies. Exports from all the countries except the Philippines fell between 1996 and 1998. The Philippines was different because its export prices dropped sharply before the downturn and it relied heavily on US multinationals and US markets less affected by it.

Capital inflows, over-investment and capacity, and vulnerabilities. The better investment climate and opening-up of the financial sector led to unprecedented net capital inflows into these countries. They rose more than tenfold in Indonesia in the 1990s, from less than $1 billion in 1989 to close to $11.5 billion in 1995. FDI growth, especially in EO investments, were spectacular. In 1992, the Philippines began getting capital inflows. It did not receive as much as its Southeast Asian neighbours due to its later start, but FDI did rise there from less than $1 billion in the early 1990s to 1.3 billion in 1995-96, while short-term capital reached $1 billion in 1994. The recovery of economic confidence was important to attract remittances from Filipino workers overseas which increased from $2.5 billion in 1992 to almost $7 billion by 1997 (World Bank, 2000*c*).

Thailand was the main recipient of the new inflows of FDI, which increased 15-fold between 1985 and 1990 and played a big part in the export drive from the mid-1980s to the mid-1990s. Other capital flows grew significantly too. Portfolio capital surged in 1993 and exceeded FDI over the next four years. Financial liberalisation greatly helped all this. Bank and other loans began to increase in 1989 and became the main element in the capital account.

Incentives to improve infrastructure, the relative price appreciation, asset price inflation and over-liquidity in the financial system due to the large capital inflows played their part too. There was also a bias towards non-traded goods such as construction, property, and infrastructure. In Malaysia, capital inflows channelled through the stock market and banks financed the growing current account deficit caused by the increasing production of non-tradables using imported inputs (Jomo and Lee, 1999).

Macro stability. Before the crisis, there was broad macroeconomic stability. Inflation had grown during the boom years but remained manageable. The exchange rate was either fixed, as in Thailand, or under a managed float system that moved with the US dollar.

Labour and wages. Labour's share in the agricultural and primary sectors declined and increased in manufacturing, with its higher real wages. In Malaysia, the proportion of workers in agriculture fell from 36 to 18 per cent between 1985 and 1995, while those in manufacturing went up from 15 to 26 per cent. Manufacturing productivity rose faster than agricultural, as did nominal wages in manufacturing and services. Labour markets tightened in all the economies. In Malaysia, demand for labour, especially unskilled and blue collar, was big enough in some sectors to import workers from Bangladesh, Indonesia and the Philippines.

Financial Crisis 1997-98

The major factors of the crisis were large current account deficits financed by short-term flows, making East Asian economies vulnerable to sudden reversals; a weak financial sector due to inadequately-regulated liberalisation and lack of legal and institutional support; and heavily-leveraged corporations with currency and maturity mismatch. Contagion, interaction of macroeconomic, financial and corporate weaknesses and early errors that undermined confidence, along with the political and social crisis, all made things worse, demonstrating the fragility of an economy integrated with international capital markets and the importance of transparency, corporate governance and sound macroeconomic policies and financial institutions.

The financial crisis severely affected these economies in 1998-99, especially Indonesia, which is recovering with difficulty. But none of them responded by slowing down globalisation. Thailand and Indonesia have continued a broad structural reform programme largely imposed by IMF bail-out packages. Malaysia refused such a package and took steps to reduce its vulnerability to external shocks and short-term inflows and outflows. It also delayed tariff reduction in the automotive sector under the AFTA programme but did not raise tariffs.

The economies either contracted or grew very slowly in 1997-98. But all of them, except Indonesia, grew in 1999 and seemed to be recovering. Indonesia, plagued by political uncertainty, had zero growth in 1999 and expected growth of around 4 per cent for 2000 without any certainty of this continuing. Investment shrank much more than consumption in all four countries and all had massive capital outflows (World Bank, 1998).

IV. THE LINK BETWEEN GLOBALISATION AND SOCIAL IMPACT

Recent studies of the effect on poverty and income distribution of opening up the economy to goods, services and investment say globalisation by itself probably does not boost growth or reduce inequality and poverty. The outcome depends on a country's endowment, initial conditions, geographic location and policies accompanying the opening up. Looking at 18 Asian countries, Dollar and Kray (2000) said economies that liberalised after the 1980s had higher growth rates, no big change in household income inequality (implying that the income of the poor also rose) and less poverty. Some groups lost in the short run and the authors say safety-net programmes might ease the transition for them. Other studies say opening up trade and investment did not produce higher growth (Rodrick, 1999) and that macroeconomic policies and investment are what matters. So a combination of policies produces growth and the kind of growth that leads to better social results. Countries should pursue liberalisation and openness as part of an equitable development strategy that helps the poor.

Southeast Asia is an example of more open policies producing growth and reducing poverty. But disparities between regions, urban-rural, ethnic groups sometimes worsened. Inequity narrowed in Malaysia and Indonesia and widened in Thailand during the IS-based rapid-growth period. Malaysia and Indonesia managed to reduce inequity with policy packages that went beyond trade liberalisation and incorporated rural development.

Poverty reduction in East Asia has mostly been due to growth, which accounted for 70 per cent of it in Indonesia between 1978 and 1984, with the rest caused by better distribution. Greater distribution inequity can offset growth's reduction of poverty and even increase it, as in Thailand between 1975 and 1986 and the Philippines between 1988 and 1991.

So globalisation and liberalisation are not an end but a means to achieve growth with equity and complementary policies are needed. Piecemeal reforms do not work. Problems surfaced in the boom years as the broader financial and capital flows sector reforms were done without the right institutional and legal frameworks.

Inequality was rising in some economies even before the crisis but the broad-based growth during early globalisation raised all incomes enough to stabilise or reduce inequity. Its rise in the more recent phase of globalisation, spurred by capital inflows and the boom that preceded the crisis, shows rapid growth benefited towns much more and increased inequity. Social policies should then have been introduced to reduce inequity through access to assets, capital and education. The crisis has corrected this in that it hurt those who had benefited most from the boom.

Why has the experience of Southeast Asian countries varied and what is the role of initial conditions, the policies pursued and other factors?

Initial Conditions

Natural resources and a farm sector absorbing much of the population made for good initial conditions in these countries. Revenue from commodities, especially oil in Indonesia and Malaysia and agricultural exports in Thailand, was the main factor in early development, bringing in foreign exchange to pay for imports for industrialisation. The absence of a tax base at first meant it was also a major source of budget revenue through resource rents and taxes. The economy grew and poverty began to decrease. The resource sectors were usually away from industrial and urban areas, which often helped to make growth more geographically balanced, as shown during the Indonesian crisis. A massive exchange rate drop combined with rising prices and strong external demand managed to boost exports of several agricultural items, mainly benefiting areas outside Java.

Initially unequal distribution sometimes points to the later shape of inequality and poverty reduction. The four economies all started off with unequal distribution of income, land and capital, based on regions, sectors and ethnic groups. Thailand and Malaysia had the sharpest disparities, with the growth and income focused on Bangkok and the central district and Malaysia's poor being Malay and rural.

Growth has always focused on Bangkok and this continued with the rapid growth and structural change that resulted from meshing with the world economy, thus perpetuating distribution inequality which increased up until 1992. Bangkok and the central district accounted for 15-20 per cent of the population during the globalisation period, but about 50 per cent of GDP in the 1980s and 55 per cent in 1987-91. This was to the detriment of other areas, notably the north and north east, where government investment was not enough to redress the balance.

Such differentials have narrowed in Malaysia because of government efforts at redistribution, without which the urban-biased trade and investment policies would have sharpened the inequity, even as poverty declined. Agricultural and rural infrastructure promotion also helped.

Korea is a good example of the advantage of starting out with good income distribution. The destruction caused by the Korean War and the land reform that followed it meant that as Korea began to switch to EO strategy, income distribution was quite fair, so high growth could be pursued without groups fighting over the benefits.

Macroeconomic Policy

The macroeconomic policy these countries and those in Northeast Asia adopted in the process of globalisation aimed to attract investment through stable prices and exchange-rate movements and sensible monetary and fiscal policies. Budget deficits financed by excessive foreign or domestic borrowing were mostly not a problem. Stable prices, especially of food, helped the poor and inflation was curbed for most of the period, unlike what happened in Latin America.

Fiscal policy has more of a role in expenditure since Southeast Asia's level of development makes it hard to use taxation to redistribute. Government efforts through major tax and transfer programmes can harm growth, as in Latin America. East Asian governments focused instead on infrastructure and human capital investment.

Fiscal and expenditure policies in the 1980s and early 1990s in Thailand aggravated inequality. The rice export tax (abolished in 1985) transferred income from country to town, widening the gap between them. Chalongphop *et al*. (1999) said personal and corporate income taxes were progressive between 1986 and 1994 but indirect taxes — the bulk of total revenue — were regressive. The government did not transfer real income to the poor in the form of social services. Chalongphop *et al.* (1999) found better-off households got a bigger share of expenditure on education and health as well as on rural, transport and communications infrastructure. All the governments spent money on social and rural development, with mixed results.

Development Approach and Policies

The IS phase

IS strategy created jobs, but only in the towns. At first, the bias against agriculture and exports and the protection of IS goods meant urban areas gained more from growth. It increased inequity according to the pattern of rural-urban migration and rural development and redistribution policies.

The concentration of export manufactures and IS industries in urban areas brought people in from the countryside. In Malaysia, this was from the less-developed states in Northern Malaysia to the west-coast towns. Remittances from urban workers to their rural families were important in reducing inequality and poverty, as well as improving income distribution where rural development programmes failed to do so.

In Thailand, industrial concentration in the Bangkok area increased inequities. Until the late 1980s, the protection structure was biased against exports and farm products, so the benefits of growth were not widely shared. This outweighed any positive effects of industrial decentralisation and promotion of small industries. Resources went to manufacturing, financial institutions and real estate in towns at the expense of agriculture and rural areas.

The IS bias towards capital-intensive production also led to unemployment. So despite achieving growth during the IS phase of their industrialisation, the Philippines did not see poverty decline much up to the mid-1980s and Malaysia, Indonesia and Thailand saw a rise in inequity, at least for the first phase of IS. The subsequent divergence between Malaysia and Indonesia, where inequity began to decline, and Thailand, where it continued to increase and even offset growth's reduction of poverty, seems to be due to rural development and redistribution policies, such as the NEP in Malaysia, which aimed at narrowing the gap between regions or ethnic groups.

In Indonesia, urban poverty declined faster than rural poverty in the early IS period, which coincided with the start of the oil boom. City-dwellers and people in oil-related sectors benefited more than those in the countryside. The trend reversed in the late 1970s as rural poverty declined faster than in the towns, with the government using oil revenues to reduce poverty and boost redistribution.

The main government policies were food price stabilisation, rice self-sufficiency, new technology that raised farm incomes, new production in processing and marketing farm products and drawing rural labour to the non-traded sector in the towns, such as construction. Oil revenues were used to develop rural infrastructure, promote rice self-sufficiency to help offset the damage to agriculture from the rise in the real exchange rate, and to provide basic education and health. The rice self-sufficiency programme, with its production subsidies, price stabilisation and high protection, was particularly important and helped the poor in both town and country. Better physical infrastructure and a flexible labour market encouraged migration to the towns and devaluations in 1978 and in the 1980s boosted farm exports.

First Phase of Export Orientation (EO)

The Southeast Asian countries opted for EO industries in line with their comparative advantage of having unskilled labour or being resource-intensive. In Northeast Asia, there was much more government intervention to identify strategic sectors with future comparative advantage. Southeast Asia was also more open to foreign investment and labour, relied more on capital markets early on and had stronger trade and investment ties with the East Asian region.

The first phase of EO in Northeast and Southeast Asian countries featured rapid growth of unskilled labour-intensive exports, bigger demand for non-agricultural labour and rising wages. In Southeast Asia this created jobs mainly in urban areas, but in China (Taipeh) and Korea it was much more widely dispersed, forged stronger rural-urban links, produced a broader share of the benefits of industrialisation and a more solid decline in inequity.

Since the 1970s, agricultural labour in Malaysia has shrunk, along with the number of families working on farms. Peasants fell from 53 per cent of the total workforce in 1970 to 36 per cent by 1985 and then slumped to 18 per cent by 1995. The labour has been absorbed in manufacturing as well as services and includes more women. So the share of wages in household income rose fastest among the urban poor, reducing inequity and poverty in the towns.

Poverty and inequity declined faster in Thailand in the early 1990s as EO industrialisation gathered speed. In just five years, a fifth of the labour force left the land. The tight labour market quickly pushed up real wages and enough money flowed back to the countryside as remittances to sharply reduce poverty there.

Rising wages between 1992 and 1996 and a tightening labour market lured some workers from the more unskilled labour-intensive textile and footwear sectors into technology-based industries (electronic, electrical and automotive). The fastest-growing sub-sectors from the late 1980s were not labour-intensive industries, but capital-intensive technology-based ones funded by multinationals, along with banks, financial institutions, insurance and real estate. They sharpened inequality since the demand was for skilled labour and most poor people only had primary education (Phaipongchit and Sarntisart, 2000).

Job creation through the EO manufacturing sector helped the rural and urban poor in the Philippines to boost their standard of living. The shift from agricultural jobs to work in manufacturing, commerce and the public sector was the main source of economic advancement for poor households (Bhalla and Kharas, 1992). Even the large unsuccessful public investments during the second IS phase in the early 1980s managed to provide the structural change the economy needed, boosting migration to the towns and reducing dependence on farms for jobs.

Indonesia's non-oil export boom from the mid-1980s transformed the labour market. Driven by the rapid growth in labour-intensive exports, job growth in the manufacturing sector tripled from 3 per cent between 1980 and 1986 to 9 per cent between 1986 and 1997. Agricultural jobs were fewer. EO industrialisation also increased jobs in the formal sector and in the towns where, since the mid-1980s, employment has grown much faster (nearly 11 per cent 1986-97) than in the countryside (0.5 per cent). The formal sector also grew much quicker than the informal. All this meant a faster decline in urban poverty compared with rural.

Real wages paid to Indonesian women in all sectors rose more rapidly than men's during the boom years due to more women working in the formal sector, plus longer hours and higher minimum wages.

In the Philippines, the inward-looking IS policies up until the 1970s led to growth based on inefficient capital accumulation and much lower absorption of labour (World Bank). The switch to an outward-looking policy, especially of unskilled labour-intensive exports, produced much more solid growth based on capital accumulation and mobilisation of labour. Jobs grew by 2.8 per cent a year between 1980 and 1998 and unemployment fell from 45 per cent in the mid-1970s to about 35 per cent in recent years.

The Boom Years Before the Crisis

The second phase of EO, combined with greater openness to capital flows and liberalisation of the financial sector, seems to have been less equitable. The stronger growth in towns and non- traded sectors, and the switch from unskilled labour-intensive to more skill and capital intensive exports, led to widening disparities. Demand for skilled labour is increasing faster than for unskilled and real wages for skilled, managerial and professional workers are growing twice as fast as those of unskilled workers, thus increasing the income gap.

By the mid-1990s, the unskilled labour market was tightening in all the Southeast Asian economies. Malaysia responded by importing foreign workers and in 1995 had about two million — 15 per cent of them unskilled labourers from Indonesia and Bangladesh. There is no clear evidence that they increased inequality by changing the age or distribution of the population and workforce or by taking the benefits of rapid industrialisation away from local workers. Availability of foreign workers might discourage employers from modernising production or training workers, thus keeping wages and productivity low. While foreign workers have clearly boosted Malaysia’s export competitiveness, there are signs their presence is in fact increasing poverty.

Supply Responses: Education Policy and Investment in Human Capital

Public spending on human capital, especially provision of basic health and education, is a key part of all these economies' efforts to help poor youths get jobs and improve themselves, thus increasing productivity and income. It played a big part in the sustained high growth of East Asia in the late 1980s and early 1990s. But investment in education varied throughout Southeast and Northeast Asia. (Booth, 1999).

China (Taipeh) and Korea prepared their labour force for new economic structure and needs, but the four Southeast Asian economies focused on primary education (Booth, 1999). The percentage of workers with only primary education or less was still surprisingly high there into the late 1980s. This difference matched the different EO approach of the two regions, with Northeast Asia concentrating on its future comparative advantage and Southeast Asia on its present one. Southeast Asia also did not pay much attention to secondary education and above because it was worried about having too many educated unemployed.

Southeast Asia's focus on primary education was no problem during the first phase of EO because unskilled labour was needed to produce labour-intensive exports, leading to reduction in poverty and sometimes inequity. But the second phase of EO required more skilled labour, so education began to matter. The universal primary education policy led to greater inequities because the scarcity of skilled, more educated labour meant the wages of such workers rose much faster than those of the unskilled. So more education is not just important for getting a job at different stages of opening up, thus reducing poverty and inequity, but is also a source of mobility for the poor to raise their incomes.

Thailand focused until 1990 on primary and tertiary education, so by the late 1980s, only 10.5 per cent of the labour force had secondary or vocational education and earnings were accordingly low. They could not afford secondary education for their children, who were often needed anyway to help with farm work or earn additional income. Secondary school enrolment sharply increased when policy changed in the 1990s but has not yet significantly affected the labour market. Those so educated however are getting higher wages, thus increasing inequality (Phongpaichit and Sarntisart, 2000.

Unequal access to education is one of the root causes of inequality in Thailand. Households below the poverty line in 1986, 1990 and 1994 got a very low share (14-23 per cent) of the direct benefits of government education spending, compared to those above it (who got 75-86 per cent), and this inequality increased over time and hampered social mobility. Only 14 out of 100 farmers' children of secondary age (12-17) were at school in 1985 and less than 2 in 100 at tertiary level. In middle and upper income families, 96 out of 100 secondary age children were at school, and 58 out of 100 at tertiary level (Chalongphop *et al.* 1999, as quoted in Phongpaichit and Sarntisart, 2000).

The Philippines achieved universal primary enrolment in 1970, much earlier than the other Southeast Asian countries, but access and quality have declined and about two-thirds of children drop out. The figure varies regionally, with nearly 100 per cent graduating in Manila and less than 30 per cent in Mindanao and Eastern Visayas. The level of basic knowledge has also fallen and there are rural-urban differences. The school system is socially regressive since poor children only have access to public schools, where quality is lower and parents are still expected to pay a third of the cost (World Bank, 2000).

Helping access to education and even affirmative action, as in Malaysia, were important in reducing poverty and inequities, especially in the first phase of EO where unskilled labour was being used. In Malaysia, the NEP also used education to get more Bumiputeras (Malays) into the higher-paid modern sector through enrolment quotas, scholarships and other aids. When the NEP ended in 1990, there were almost as many Bumiputeras as non-Bumiputeras in secondary schools and they were a majority in tertiary education. The government also provided basic health and education to rural and poor households (Zin, 2000). These education policies had different effects. Before the crisis, Malaysia and Thailand had a general labour shortage that was being met by importing foreign workers. In Indonesia and Philippines, unemployment among educated urban youth was high and becoming a social problem.

Agriculture and Rural Development

Tackling rural problems are important in distributing growth more evenly in the predominantly rural poverty of East and Southeast Asia. Poverty is closely tied to lack of access to farmland and where there were non-agricultural job opportunities, there was less of it (Booth, 1999). Once again, things were different in China (Taipeh) and Korea, where policies associated with its EO strategy led to strong urban-rural linkages and continued agricultural growth. Non-farm jobs in the countryside grew quickly because EO strategy was not confined to towns. Pushing fairer access to land, equal distribution of rural income and better rural infrastructure also helped[2].

Korea and China (Taipeh) had similar agricultural growth rates to East and Southeast Asia, but non-agriculture rural incomes grew much more slowly in the latter. In China (Taipeh), they increased three times faster than agricultural incomes between 1962 and 1980. But in Thailand and Indonesia, they grew slower and in Indonesia only increased 22 per cent faster in the 1983-93 period. In the Philippines, they grew at the same rate as China (Taipeh) for the same level of development, but while non-agricultural incomes grew three times faster than agricultural, they still grew much slower than in China (Taipeh).

Agricultural jobs did not fall sharply in Southeast Asia as they did in China (Taipeh). At similar per capita GDP levels, a far bigger percentage of rural workers were farming in Southeast Asia.

These differences were due to the more skewed income distribution and more capital-intensive urban-biased industrialisation in Southeast Asia, with its much weaker link between non-farm jobs in rural areas and agricultural growth. Most new jobs in Southeast Asia were in factories and towns. The proportion of non-agricultural service jobs was also much higher than in Northeast Asia. The services sector is much more diverse with a greater range of pay, so as people leave agriculture for poorly paid services work the overall distribution of earnings is going to be more skewed than in Northeast Asia.

The capacity of Northeast Asian economies to draw workers from farms to factories appears to be due to their EO drive, but Southeast Asian economies had a similarly-open (exports over GDP) EO drive. Other factors seem to make manufacturing more labour-intensive and spread out (beyond towns) in China (Taipeh) and Korea, one of them perhaps being lower reliance on foreign investment in EO manufacturing than in Southeast Asia (Booth, 2000).

Another key difference between the two regions is the degree of agrarian reform. In the Philippines, it was only partly successful. Other Southeast Asian countries focused on labour-intensive rural works programmes and Malaysia and Indonesia had resettlement programmes to boost the incomes of the landless. Southeast Asia also has much less land in small plots and a higher proportion than China (Taipeh) of plots over five hectares. These programmes helped create rural jobs but were not comprehensive and improvements did not last (Booth, 2000).

Poverty was reduced in rural Thailand by extension of the land frontier and rising crop prices over the past 20 years. Big farm price changes, often from outside, drove income disparities up and down (Pongphaichit and Sarntisart, 2000). But a major policy weakness was to increase agricultural output by expanding arable land instead of improving yields. Also, when land was converted to more productive use such as manufacturing or real estate, the shrinking amount of farmland curbed growth. The benefits of farming in the past were unevenly distributed in the countryside, which is still very poor. (Vimolsiri, 2000:289).

Thailand did not have a clear rural development plan until 1982 and in the late 1990s switched to decentralised rural growth, which improved the quality of life more than it reduced poverty and income inequality (Vimolsiri, 2000:290).

Malaysia's rural programmes provided infrastructure, land development and rehabilitation, institutional and agricultural support services and subsidies (training, subsidised credit and inputs), rural industrialisation and basic social services such as health and education (Zen, 2000). They reduced poverty and boosted rural income but did not improve distribution much because they benefited the better-off rather the poor due to targeting problems. The paddy support policy has raised farmers' incomes and cut the risks of growing paddy. But the cash subsidy made farming more profitable and larger farmers bought up small farms, displacing owner-operations and tenants and swelling the number of landless labourers. Also, 60 per cent of those receiving price subsidies received only 12.5 per cent of the total. The cash subsidy induced farmers to sell all their output rather than keeping some for their own consumption and milling it themselves. Small rice mills went out of business. Protection of the rice sector also penalises the poor since prices are higher and paddy farmers become dependent on subsidies.

For rubber smallholders, the replanting tax was the same as for big plantations, yet the benefits of replanting and research funded by the taxes could only be enjoyed by the plantations. The replanting grant was only available after replanting had been done. (Zin, 1999).

Malaysia also failed to deal with landlessness. It did not redistribute cultivated land, but opened up large tracts of new land and then gave plots to the landless to grow high-value crops using modern techniques. But this relied on a large bureaucracy and private land contractors, so the policy cost far more than the small number of beneficiaries justified (Zin, 1999).

Indonesia's oil boom saw rapid urban growth and in the early 1970s inequities increased. Drought in 1971 meant a large amount of rice had to be imported. This and a developmental policy approach led to emphasis on farming and the countryside. Oil revenues were used to build rural infrastructure and fund rice self-sufficiency, which improved rural incomes and reduced poverty. The harm done to agricultural exports by the higher real exchange rate during the oil boom also had to be tackled. Cash crops such as palm oil were encouraged with credit schemes. So when oil prices collapsed, agriculture still thrived, unlike in some oil-exporting countries such as Nigeria, which went from being an exporter of palm oil to being an importer because the farm sector had been neglected during its oil boom.

Social Policies

Redistribution of Assets

Unequal access to land and capital are often sources of inequity. The four countries had mixed success trying to correct this for rural households. Malaysia and Thailand opened up new land, but none of it was transferred from rich to poor. Malaysia had the most comprehensive redistribution policy, called the New Economic Policy (NEP). Set up to tackle extreme imbalances in wealth distribution, as well as ethnic-based poverty, it seemed to be successful by dealing with the human capital issue, rather than just redistributing land and wealth, and the target group was able to develop skills to make best use of their assets. The NEP averted political tension and instability. Its asset redistribution was less successful, plagued by abuses and caused distribution imbalance among Malays (see box).

Malaysia's New Economic Policy (NEP)

The NEP was introduced after ethnic riots in May 1969[3] as an affirmative action plan to help the poor Malay population. It aimed at correcting ethnic inequities and, along with positive discrimination in education, redressing asset imbalances in every sector of society. The target was for Bumiputeras to own and run at least 30 per cent of all commerce and industry.

Capital was to be increased in several ways — reserving shares for Bumiputeras that were acquired by the Bumiputera Investment Fund and by public agencies set up to buy stock in trust for eventual sale to individual Bumiputeras. This boosted the Bumiputeras' share of capital from 2.4 per cent in 1970 to 20.3 per cent by 1990. Non-Bumiputeras owned 46 per cent and foreigners 25 per cent. The new rural land development scheme also mainly benefited Bumiputera households.

Other programmes focused on human resource development, capacity building and facilitation, including Bumiputera quotas for school enrolment, scholarships and education subsidies (including for study abroad) and promoting small and medium-sized enterprises through training, credit assistance and subsidy, a guarantee scheme, advisory and extension services, technical help and direct government participation in the private sector.

Social Security and Welfare Programmes

None of the four Southeast Asian economies had catch-all social security and insurance schemes to cushion unemployment, disability and ageing, though each had some kind of safety-net as well as special programmes for the poor. Government workers in China and in big firms in Korea are covered. But people still relied more on informal means such as friends and relatives.

Malaysia aimed by the end of the decade to eliminate hard-core poverty — those earning less than half the poverty line level. A third of the government's total expenditure goes to education and health and the hard-core poor get free housing, food subsidies, grants, agricultural help, child nutrition help and scholarships (World Bank, 1999).

Thailand introduced an integrated social protection programme before the crisis, including health insurance for the poor and near poor, loans for secondary school students, vocational training and labour-intensive public works schemes. But the system was not very effective, contained no unemployment insurance and only covered formal sector workers. (World Bank, 1999).

The lack of special programmes for workers and the poor was felt during the recent economic crisis in the four countries. Indonesia and Thailand were the most affected and, helped by multilateral agencies and foreign donors, introduced temporary social safety-net schemes, as did Malaysia and the Philippines.

The safety net programmes aimed at protecting spending in key sectors such as education and health by supplying food and jobs, but setting them up hastily made them less effective. Most countries tried to improve information by conducting surveys and monitoring the impact of the crisis, helped by NGOs. All tried to maintain health and education spending once the IMF agreed to allow fiscal deficits instead of requiring fiscal austerity and budget surpluses. This worked fairly well except in Indonesia, where high inflation meant real expenditure actually declined and political problems often delayed disbursement.

Because of weak bureaucracy and fear of leakages, different mechanisms were used. Indonesia avoided cash transfers and used specific interventions, food security was important in the Philippines and Indonesia and NGO participation was very important. All used public works programmes to create jobs. Community investment funds also aimed to create jobs and generate infrastructure projects. None of the countries offered unemployment insurance.

All increased severance payments and encouraged self-employment. Indonesia offered cash and goods in-kind (rice) and a targeted rice subsidy programme to replace the general one, as well as scholarships and cash to stay in school. Thailand offered low-income health insurance (World Bank, 1998).

But these measures could hardly be effective with the limited resources and institutions available and government inexperience. In Thailand, the worst hit were younger, less educated workers in rural and small firms. But only a few workers got severance pay. The crisis seems to have reversed in one year all the gains in income distribution made over six years of boom.

People ultimately relied on informal means, such as extended family, informal credit networks, community projects, charity in Buddhist temples and, among Chinese, clan groups, associations and foundations. Without these, poverty and income distribution might have been even worse. The situation was similar in Indonesia (World Bank, 1998). The post-crisis debate in these countries is what sort of permanent social safety net there should be.

V. CONCLUSIONS: LESSONS LEARNED, CHALLENGES AND THE WAY FORWARD

Lessons Learned

Before the crisis, annual growth in Thailand, Indonesia and Malaysia for the last two decades, and the Philippines in the 1990s, was above 5 per cent and absolute poverty was falling. There is no discernible relationship between growth and equity however and the record on inequality is mixed. The Kuznets conventional wisdom that inequity tends to increase and then decrease with economic development was true for perhaps only one of the countries, Thailand. But inequity changed little in the Philippines until recently and in Malaysia and Indonesia it declined for most of their growth period, although there were bursts of increases in inequality.

There is no definite evidence on how globalisation affects growth, equity and poverty. The problem is that growth affects equity and vice-versa. Initial conditions as well as policies have an impact on both growth and equity and it is hard to say which combination of policies best promotes them. The same set of policies interacting with different initial conditions and institutions may have different results. But Southeast Asia does offer lessons.

Globalisation — greater integration with the world economy — will bring higher growth, more jobs and greater productivity and reduce absolute poverty. The Southeast Asian experience also supports the conventional wisdom of a broad-based strategy for reducing poverty and inequity as extensive as it was in these countries in the 1970s and 1980s. The main aspects in this broad-based strategy in Southeast Asia are found elsewhere too.

1) At all stages of opening up, sound macroeconomic conditions, especially price stability, are key for reducing poverty and inequity. Monetary policy should promote low and stable inflation, but must go with pro-cyclical rather than counter-cyclical fiscal policy. When a crisis, such as the recent one, is caused by a collapse in domestic demand, fiscal policy should not be tightened. It does not redistribute income and plays more of a redistributive role through government spending priorities. All these countries have provided basic social services, funded physical and social infrastructure for areas or groups that benefit less from growth and boosted human capital through education and health services. The question is how good and how effective they are.

2) Since most poor people and workers still live in the countryside, the steady decline in absolute poverty due to industrialisation shows the need to incorporate rural improvements into the development strategy. Focusing on agriculture reduces rural poverty and narrows the distribution gap between town and country. But Southeast Asia did not have the Korean and China (Taipeh) experience of an EO strategy accompanied by a spread of industrialisation to rural areas, increased rural-urban linkages and rapid increases in non-agricultural employment, especially in the countryside. In Southeast Asia, industrialisation and most agricultural and rural development policies did not benefit the rural poor or reduce inequities as much as one might expect.

3) Globalisation and competition mean rapid changes in sectors and in demand for skills and know-how, so flexible labour markets are important. In Southeast Asia, flexible labour markets and a pool of unskilled labour have been able to respond to the needs of the labour-intensive export orientation (EO) drive. But all the countries were hampered in the second stage of EO by the lack of skilled labour and countries either imported foreign labour or educated the workforce. Southeast Asia did not move as fast as Northeast Asia to educate its workers, so while labour markets are relatively flexible, the result is still growing inequity due to the sharp rise in wages of skilled labour compared with unskilled.

4) The recent financial crisis showed how external shocks can interact with domestic vulnerabilities and lead to an economic crisis with dire social consequences. The Southeast Asian countries were unprepared for the huge crisis of the system because they had no social safety-net or income transfer programmes, and lacked administrative capacity and information and co-ordination. The crisis also showed that weak institutions are the main block to providing social services. Thailand and Indonesia had the money but could not fully transfer it to social safety-nets and social programmes because they could not quickly create and expand new ones. Public works job creation did not do well in Indonesia due to poor targeting, management and accountability, but worked in Korea because of better design and implementation (World Bank, 1998).

5) Inequality, especially its rise in the recent boom period and rapid globalisation, is caused by much higher growth (including real wages and incomes) in towns among the skilled and in the modern capital-intensive sector. This is due to the urban focus of industrialisation with little rural-urban linkage, to levels of education and unequal access to it, and to urban concentration of the boom's benefits (infrastructure, real estate and the financial sector).

To build capacity among the poor, there has to be equal access to education. As all these countries enter more skill and human capital intensive sectors, the need for skilled workers will increase. So broader access to good quality secondary schooling, which is also affordable for the rural poor, is important for growth and for reducing poverty and inequity.

Poverty is declining, but not equally between income groups, town-countryside, industrial and non-industrial areas and sometimes ethnic groups. Some groups still get no benefits from growth and have no access to social services or assets needed to enjoy them. A broad-based growth strategy is no longer enough and social programmes targeting groups and areas need to be added.

Social safety-nets and programmes to cope with the crisis were temporary, but the experience changed attitudes to social protection and the utility of social security or unemployment insurance was questioned. Fiscal decentralisation in Indonesia will include allocating more state funds to the governments of poorer provinces. In Thailand, a permanent unemployment insurance scheme has been dropped, but the government has announced more poverty-targeted fiscal measures (Warr, 2000).

Challenges

Southeast Asian economies face big challenges. The pace of globalisation and increased competition are not going to slacken and will probably speed up as technology changes and excess global production capacity develops. Growth will depend on keeping their economies open and taking part in globalisation, but countries have to learn to manage the risks and downside of joining the world economy. Growth will be more volatile with more openness to the external influences of trade and capital flows. Countries need to minimise this volatility with sound macroeconomic management, good governance, transparency, accurate and timely information, a sound financial system and flexible factor markets.

These countries are facing other domestic challenges as they try to soften the bad effects of globalisation, such as an increasingly old population, more people living in towns and greater political openness and democracy. Some countries, such as Indonesia, are also decentralising government, leaving it unclear who will implement social policies and how.

The crisis has highlighted the inequities of the boom years that do or could cause social rupture between regions, between centre and local, between ethnic groups and between rich and poor. This has badly damaged political stability, the investment climate and overall growth. So while growth is a key to reducing poverty and inequity, reducing inequalities is also crucial to promoting growth.

More democratic participation will bring further demands to tackle inequity by providing greater access to education and opportunity, programmes for targeted groups and redistribution of assets or wealth. Governments will be hard pressed to respond. Short-term, politically expedient but ineffective measures should be avoided as they could damage growth and efficiency. Redistribution programmes are hard to implement quickly and if badly planned could discourage effort and create costly bureaucracies.

The Way Ahead

What Should Countries Do?

Governments are now tackling poverty not just because they get aid international aid to do so but because of greater demands by civil society. Political openness produces more pressure to ensure income redistribution to the poor and those excluded from the benefits of development.

Broad-based growth is still essential for reducing absolute poverty, as cross-country econometric studies have shown (Ravallion and Chen, 1997).

Providing physical capital and infrastructure, investing in human capital (education and health) and policies to allocate resources efficiently, including labour-intensive production, are all necessary, but quality is key. Government promotion of solid development of rural areas driven by the private sector, especially through creating non-farm jobs, is important. So better rural infrastructure and urban-rural links are more important than subsidised credit or inputs. There are bound to be losers and pockets of poor people that are not reachable, so special policies are needed to help them escape their poverty trap.

Other key issues are promoting opportunity, empowerment and enhancing security (World Bank, 2000/1). Opportunity has to be created by investing in three kinds of assets. The first is physical infrastructure to ensure goods and services get from isolated rural areas to the market. The second is human capital since the earning power of the poor depends on equal access to good-quality education and health services, which also boosts their ability to cope with change, switch jobs and survive crises and shocks. Better education and health are only weakly related to public spending on it, so simply increasing budgets will not help. Reallocating public spending and making it more effective can improve things, especially when public resources are subsidising education for the wealthy (World Bank, 2000). The third asset to be invested in is natural resources, through looking after the environment.

Empowerment within and between countries to ensure social inclusion and political democracy is on the rise. Social policies must now involve the wider community, not just governments.

Finally, people must feel secure, helped by government policies and institutions that reduce volatility and vulnerability to economic and physical shocks. This is done through sound macroeconomic policies, a stronger financial system, corporate governance, transparency and the rule of law. Also through social safety-nets. Should these be more formal? The focus right now is on reducing volatility and the shock potential of another crisis. But demographic shifts, along with more urbanisation and formal-sector workers, will eventually require more formal government schemes.

Table 7. **Changes in Industrialisation Approach, East Asia**

	1950s	**1960s**	**1970s**	**1980s**	**1990s**
	1953-7	1958-80		1981-	1986-
Taiwan	IS	EO			Liberalisation
		1961-72	1973-79	1980-	1990s
Korea		EO	IS (Heavy Ind)	Liberalisation (Strategic Industries)	Internationalisation (Information Ind)
		1961-71	1971	-86	1986-
Thailand		IS	add EO	"81 Capital Goods	EO
	1950-70		1971	-85	1986-
Malaysia	IS (moderate)		Add EO Add IS heavy ind.		Liberalisation
		1967-73	1974	-85	1986-
Indonesia		New order Liberalisation	IS Some EO		EO Liberalisation
	1950-		1970s	1980s	1986-
Philippines	IS	strengthened		Liberalisation (political instability)	strengthened (political stability)

Note: IS is import substitution and EO is export orientation.
Source: Adapted from Table I.1 in Masuyama *et al.* (1997)

Table 8. **Growth and Structural Change**

	Indonesia	Malaysia	Philippines	Thailand	China	Rep Korea
GDP Growth						
1970-79	7.6	7.6	6.3	7.2		9.5
1980-90	6.1	5.3	1.0	7.6	10.2	9.4
1990-96	7.8	8.7	2.3	8.4	12.8	7.2
1997-1999	-3.0	1.8	2.6	-2.4	7.9	3.3
Av. Annual Gr						
Industry						
1980-90	6.9	7.2	-0.9	9.8	11.1	12.1
1990-95	10.1	11.0	2.2	10.8	18.1	7.3
1990-99	7.8	9.4	3.4	6.7	14.4	6.2
Agriculture						
1980-90	3.4	3.8	1.0	3.9	5.9	2.8
1990-96	2.9	2.6	1.6	3.1	4.3	1.3
1990-99	2.6	1.1	1.5	2.7	4.3	2.1
% Agric, Manuf out of GDP						
1980	24.13	22.21	25.26	23.22	30.41	15.28
1998	16.26	12.34	17.22	11.29	18.37	6.26
Exports/GDP						
1980	34.0	58.0	24.0	24.0	6.0	34.0
1998	28.0	118.0	56.0	47.0	22.0	38.0
% Manuf X						
1983	6.0	25.0	52.0	31.0	55.0	91.0
1997	42.0	76.0	85.0	71.0	85.0	87.0
Gross Private Capital Flows (% PPP GDP)						
1988	0.6	4.2	1.3	2.8	0.6	3.3
1998	4.4	7.6	3.6	5.9	2.3	13.2
Foreign Direct Investment (% of PPP GDP)						
1988	0.2	0.9	0.5	0.7	0.3	0.5
1998	0.9	2.6	0.7	2.1	1.3	1.6
Av. Tariff						
1980	36.0	10.6	33.1	32.3	49.5	
1985	27.0	14.9	27.8	41.0	38.8	
1990	22.0	14.3	24.5	36.6	39.9	
1995	15.0	8.9	17.2	23.1	20.9	

Source: World Bank, *World Development Report* and *World Indicators*; tariff rates from UNCTAD.

Table 9. **Tariffs and Non-Tariff Measures in East Asia, 1984-98**

	Average Unweighted Tariffs		**Core Non-tariff Frequency Ratio**	
	1984-88	1994-98	1984-88	1994-98
East Asia	19.4	10.4	26.5	14.2
Hong Kong, China	0.0	0.0	2.1	2.1
Indonesia	28.4	13.2	53.6	31.3
Korea, Rep. Of	21.0	8.5	50.0	25.0
Malaysia	14.1	10.3	56.3	19.6
Philippines	28.0	16.8	11.5	-
Singapore	0.3	0.4	1.0	2.1
Taiwan	22.4	11.2	1.0	2.1
Thailand	41.2	23.2	36.5	17.5
Latin America	29.5	11.4	20.0	8.8

Source: Table 3.6 from World Bank (2000).

Table 10. **Foreign Direct Investment Flows to East Asia**
(billions of dollars)

	1980	**1985**	**1990**	**1993**	**1994**	**1995**	**1996**	**1997**	**1998**
East Asia		*4.1*	*16.2*	*42.8*	*52.6*	*56.9*	*65.5*	*71.5*	*69.9*
China		1.7	3.5	27.5	33.8	35.8	40.2	44.2	45.5
Indonesia	0.2	0.3	1.1	2.0	2.1	4.3	6.2	4.7	-0.3
Korea, Rep	0.0	0.2	0.8	0.6	0.8	1.8	2.3	2.8	5.1
Malaysia	0.9	0.7	2.3	5.0	4.3	4.2	5.1	5.1	3.7
Philippines	-0.1	0.0	0.5	1.2	1.6	1.5	1.5	1.2	1.7
Singapore	1.2	1.0	5.6	4.7	8.6	7.2	7.9	9.7	7.2
Thailand	0.2	0.2	2.4	1.8	1.4	2.1	2.3	3.7	7.0
Crisis Countries	1.2	1.4	7.2	10.6	10.2	13.8	17.5	17.6	17.2
World	*46.3*	*55.7*	*203.1*	*219.4*	*253.5*	*328.9*	*358.9*	*464.3*	*643.9*

Note: Indonesian data includes undetermined amount of debt and crisis countries are Korea, Indonesia, Malaysia, Philippines and Thailand.

Source: Table. 3.7 World Bank (2000) and drawn from UNCTAD, *World Investment Report*, various issues

NOTES

1. In the north east, the figure is 37 per cent (Agricultural Statistics, 1994/5).
2. Booth (1999:11) quoting Ranis and Stewart and Fei, Ranis and Kuo for China (Taipeh) and Korea, for the Philippines Balisacan and on East Asia Ahuja *et al*.
3. Rioting occurred after a Chinese-dominated opposition won a sizeable majority of parliamentary seats from the Malay-dominated ruling coalition.

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