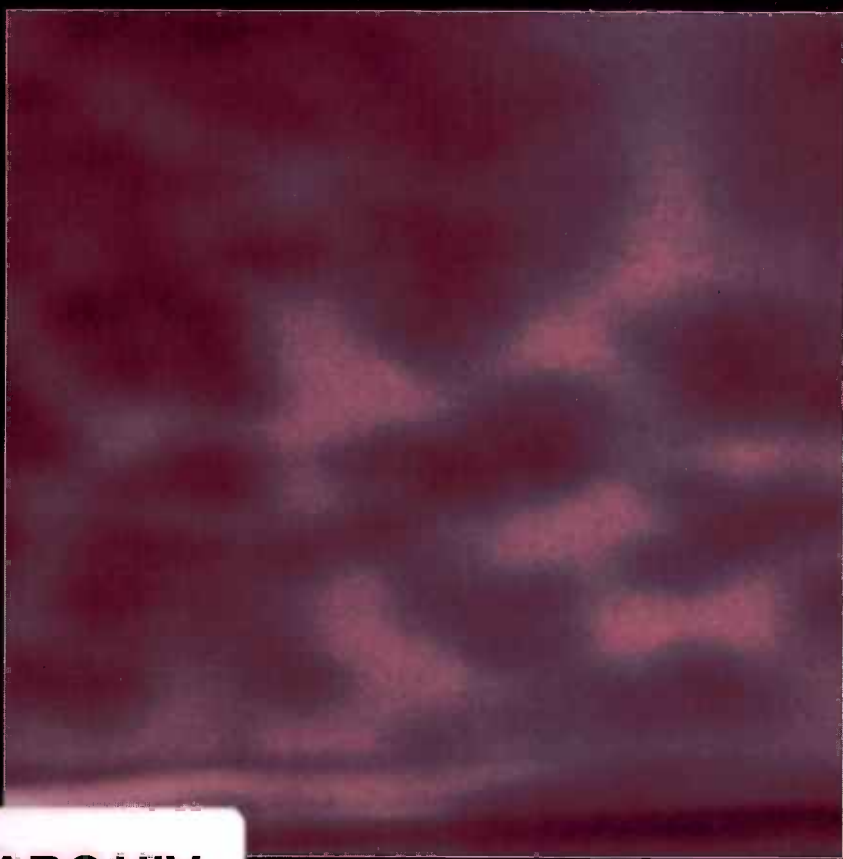


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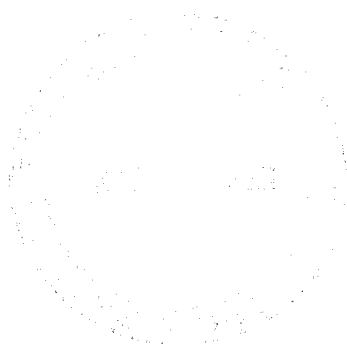
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First published in Great Britain 1998 by
MACMILLAN PRESS LTD
 Houndmills, Basingstoke, Hampshire RG21 6XS and London
 Companies and representatives throughout the world

A catalogue record for this book is available from the British Library.

ISBN 0-333-72814-9 (hardcover)



First published in the United States of America 1998 by
ST. MARTIN'S PRESS, INC.,
 Scholarly and Reference Division,
 175 Fifth Avenue, New York, N.Y. 10010

ISBN 0-312-21278-X (clothbound)

Library of Congress Cataloging-in-Publication Data
 Globalization, growth and marginalization / edited by A.S. Bhalla.

p. cm.

Includes bibliographical references (p.) and index.

ISBN 0-312-21278-X (cloth)

1. Income distribution—Developing countries. 2. Developing countries—Economic conditions—Regional disparities.
 3. Competition, International. 4. International economic relations.

I. Bhalla, A. S.

HC59.72.I5G55 1998

338.9'009172'4—dc21

97-41070

CIP



First published in Canada 1998 by

INTERNATIONAL DEVELOPMENT RESEARCH CENTRE

PO Box 8500, Ottawa, ON

Canada K1G 3H9

Canadian Cataloguing in Publication Data

Globalization, growth and marginalization
 Includes bibliographical references and index.

ISBN 0-88936-839-2 (paperback)

ISBN 0-88936-850-3 (hardback)

1. Income distribution—Developing countries.
 2. Developing countries—Economic conditions—Regional disparities.
 3. Competition, International.
 4. International economic relations.

I. Bhalla, A. S.

II. International Development Research Centre (Canada)

HC59.72.I5G55 1998

338.9'009172'4

C98-980009-1

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Paperback edition available in Canada only

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 07 06 05 04 03 02 01 00 99 98

Printed and bound in Great Britain by Antony Rowe Ltd, Chippenham, Wiltshire

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5 Growth and Poverty in East and South-East Asia in the Era of Globalization

Azizur Rahman Khan

East and South-East Asia (ESEA) is the most populous of the regions into which the contemporary world economy is typically classified. In recent decades this has also been the most dynamic region of the world economy. This chapter analyses the performance of the region during the accelerated globalization of the world economy that has taken place since the beginning of the 1980s.¹

Although the region has generally achieved a superior economic performance, progress has by no means been uniform everywhere. Four distinct categories can be identified among the main countries of the region.

The Republic of Korea and Taiwan represent the first tier of the newly industrializing economies (NIEs) of ESEA that adopted an outward-oriented strategy of development from the 1960s.² Hong Kong and Singapore are usually grouped together with Korea and Taiwan, but this study excludes these city states because they have long held the status of high-income countries.³ Their inclusion in the group would not add much to the analysis, while their status as city states means that they are often considered atypical and unrepresentative.

In the next category are the second-tier NIEs of ESEA: Indonesia, Malaysia and Thailand. Their past development strategies incorporated many elements of import-substituting industrialization (ISI), but in the years immediately preceding and during the period of globalization they made significant adjustments to their development strategies in order to become better integrated into the global economy.

The third category consists of China alone as a unique case. China was more or less insulated from the world economy until about a decade ago, when it began a controlled transition towards greater participation in world trade.

In the fourth and final category, the Philippines will be used as an example of countries whose development strategies have produced different outcomes from those of the above mentioned ESEA countries. Until at least the middle of the 1990s its performance in terms of growth and distribution was dismal.

These four groups of countries represent the principal types of ESEA response to globalization, and together the seven countries represent a third of the population of the less developed countries (LDCs). The ESEA countries that are excluded from the study are Vietnam, Laos, Cambodia and North Korea.⁴ The reason for their exclusion is that little relevant information about them is available, although it is known that in recent years Vietnam has made significant progress towards greater integration into the global economy. Furthermore its growth performance has also been very impressive, averaging 7.4 per cent per year between 1988 and 1995.⁵

As with the study on South Asia (Chapter 4), the beginning of the 1980s is identified as the approximate start of the acceleration of globalization. The main impetus for this was the removal of two major obstacles to the international movement of goods, services, capital and technology, namely the ISI strategy pursued by the LDCs and the highly autarkic policies of the centrally planned socialist economies.

All seven of the ESEA countries discussed here achieved high rates of growth in the 1970s (see Table 5.1), and all but China achieved a relatively high degree of integration into the world economy (as measured by their ratio of trade to GDP) in that period. With the exception of China and Taiwan, all the countries were hit by severe external imbalances around the beginning of the 1980s. Thus the period of globalization for these countries began with the implementation of stabilization and structural adjustment programmes. This often meant a short period of reduced growth, but apart from the Philippines they all succeeded in achieving a high average annual growth rate in the subsequent decade and a half. The growth rate of GDP actually accelerated in China and Thailand, and while it declined marginally to moderately in Korea, Taiwan, Indonesia and Malaysia, it remained very high everywhere by LDC standards. In the Philippines, the 1980s and the early 1990s turned out to be a period of sharply reduced growth in GDP. In this study Korea, Taiwan, Indonesia, Malaysia, Thailand and China – referred to as the ESEA-6 – are regarded as examples of economic success during the period of globalization on the evidence of their excellent growth performance based on their high and/or accelerated integration into the global economy.⁶

However, the record of these countries in poverty reduction is less uniform. In the 1970s the ESEA-6 made good progress towards the elimination of poverty but during the 1980s and early 1990s their progress was less uniform than in the past and by no means highly correlated with their growth performance.

The first section begins with a brief account of the performance of these ESEA countries in the period before the 1980s and 1990s. It goes on to discuss the nature of the imbalance they faced at the beginning of the period of accelerated globalization and the adjustments they made to overcome that imbalance. The second section discusses their growth and integration

performance and the role that IT played in their success. Special emphasis is placed on the first-tier NIEs. The third section analyses income distribution and poverty reduction in the 1980s and 1990s. The final section summarizes the main conclusions.

THE ESEA PERFORMANCE RECORD

All the ESEA countries achieved very high rates of growth in the 1970s (Table 5.1). During this decade the slowest growing of the seven ESEA countries, China, achieved an annual growth rate that was higher than the average growth rate of the developing world as a whole (5.2 per cent per year) and nearly three fifths higher than the growth rate achieved by South Asia (3.5 per cent per year). The most rapidly growing of the seven countries – the first-tier NIEs – achieved historically unprecedented, double-digit growth rates.

The development strategies pursued by these countries before the 1980s were not uniform, but in the 1970s all had very high rates of investment, backed by very high rates of domestic saving (Table 5.2). By the end of the decade the rates of investment and saving in all the countries were substantially higher than the LDC average. Another shared characteristic was a high level of basic human capital development. As early as 1970 these countries had attained primary school enrolment rates that were far higher than those of other LDCs at comparable stages of development: 80 per cent in Indonesia, 89 per cent in China and over 100 per cent in Korea, Taiwan and the Philippines.⁷

Over time there has been an evolution in the interpretation of the remarkable success of the first-tier NIEs of ESEA and to date there does not seem to

Table 5.1 GDP growth rates for East and South-East Asian countries (per cent per year)

	1970–80	1980–90	1990–94	1995
Korea	10.1	9.4	6.6	9.0
Taiwan	10.0*	7.7	6.5	5.9
Indonesia	7.2	6.1	7.6	8.1
Malaysia	7.9	5.2	8.4	9.6
Thailand	7.1	7.6	8.2	8.6
China	5.5	10.2	12.9	10.2
Philippines	6.0	1.0	1.6	4.8

*For the 1963–80 period.

Sources: Lee (1994); Yu (1994); ADB (1993); China, State Statistical Bureau (SSB) (1996); World Bank (1995a, 1996a); IMF (1996).

Table 5.2 Domestic investment and saving rates for East and South-East Asia (percentage of GDP)

	Investment rate			Saving rate		
	1970	1980	1994	1970	1980	1994
Korea	24	32	38	15	25	39
Taiwan	30	30	24	n.a.	33	29
Indonesia	16	24	29	14	37	30
Malaysia	22	30	39	27	33	37
Thailand	26	29	40	21	23	35
China	28	35	42	29	35	44
Philippines	21	29	24	22	24	18

Sources: ADB (1993, 1994); China, SSB (1996); World Bank (1995a, 1996a).

be agreement on the nature of its various components.⁸ It is, however, well documented that the key to their success was not an adherence to *laissez faire* policies pursued in a free market under conditions of free trade. The key element of their strategy was targeted support, through the provision of subsidized credit and other incentives, to industries identified as potentially profitable. The principal difference between the standard ISI strategy pursued elsewhere and the interventions made by these countries was that (1) ISI was highly arbitrary, resulting in randomly distributed rates of effective protection for individual activities, whereas the first-tier NIEs systematically promoted activities that were identified as worthwhile bets; and (2) unlike the ISI, these NIEs did not discriminate against exports. The protection they provided to targeted industries was outward looking in so far as the effective exchange rate for exports was frequently higher than the effective exchange rate for imports. These countries also avoided overt overvaluation of the exchange rate, which makes the adoption of universal quantitative restrictions on imports inevitable and promotes employment-restricting technology by underpricing imported capital equipment. Dependence on quantitative import controls was not so widespread and inflexible as to create serious supply rigidities and a totally arbitrary (unintended) system of effective protection.

The second-tier NIEs – Indonesia, Malaysia and Thailand – followed a strategy that was closer to ISI until late in the 1970s or early in the 1980s. But as Amsden's (1993) analysis of Thailand shows, support to industries during the ISI phase in these countries was carefully targeted to promote efficiency, and was not the arbitrary kind promoted by South Asia and many other parts of the developing world.

During the 1970s, growth in both groups of NIEs was poverty alleviating. In Korea and Taiwan this was in large part due to the initial egalitarian redistribution of land. Its effect was subsequently reinforced by the high

employment intensity of growth and the wide access to human capital. In Malaysia and Thailand too growth during the 1970s was poverty reducing, largely because of widespread access to land, facilitated by the relatively large and elastic supply. In Malaysia's case, ethnically based redistributive measures might also have helped increase access to land. Furthermore growth was highly employment intensive in these countries. In Indonesia the incidence of rural poverty increased between 1970 and 1976 due mainly to a rise in the price of rice, the principal source of food energy for the poor, on which the country was import dependent. This was brought under control by an accelerated programme of self-sufficiency in rice and complemented by generally favourable policies towards agriculture and the rural economy. Ever since, growth has been associated with poverty reduction.

China's economy grew at a slower rate than the economies of the other six countries in the 1970s, although it achieved the highest rates of investment and saving. There was widespread inefficiency of resource use, but nonetheless the economy grew at a reasonably high rate due to the sheer volume of investment. Strongly egalitarian policies, often arbitrarily imposed at the cost of reduced incentive and efficiency, succeeded in keeping down discrepancies in income distribution, but low incomes led to widespread poverty.

The Philippines achieved a reasonably high rate of growth in the 1970s aided by a high rate of capital inflow after the first oil shock. But growth was not particularly poverty reducing due to the extreme inequality of agricultural land ownership and the adverse effect of its ISI strategy on employment growth.⁹

At different times in the late 1970s and early 1980s all the ESEA countries except China and Taiwan faced serious external imbalances (Table 5.3). Korea, Thailand and the Philippines, all oil-importing countries, faced the problem earlier, mainly because of the two oil shocks. Indonesia and Malaysia, both oil exporters, faced it later, after the oil boom came to an end. While the problem of external imbalance hit Korea, Indonesia and Malaysia, emergence in the case of Thailand and the Philippines was more gradual. In

Table 5.3 Current account deficit before official transfer for East and South-East Asia (percentage of GDP)

	<i>Peak ratio and year</i>	<i>Three-year average ratio prior to peak</i>	<i>Average ratio 1987-89</i>
Korea	8.4 (1980)	2.9	-5.8
Indonesia	7.5 (1983)	1.0	2.1
Malaysia	13.5 (1982)	2.4	-4.4
Thailand	7.7 (1981)	6.4	2.6
Philippines	9.1 (1982)	6.2	2.7

Source: World Bank (1995a).

all the countries the problem reached unsustainable proportions and forced them to adopt stabilization programmes and reform their trade regimes.

China's peak rate of external deficit was only 1.8 per cent of GDP (in 1980). The country had, however, embarked on extensive systemic reform in 1979, beginning with complete transformation of the organization and institutions of agriculture. By the middle of the 1980s the focus of China's reform programme had shifted to export-led growth and rapid integration into the global economy. Taiwan's long record of external surplus was broken only twice after the first oil shock, in 1975 and 1980. The impetus for the reform of the trade regime in favour of greater openness to imports and capital flows, however, came from the pressure exerted by trading partners in the advanced industrial countries.

Thus the accelerated globalization of the world economy in the 1980s coincided with the widespread reform of the trade regimes and economic policies in the ESEA countries. Korea and Taiwan liberalized imports, a policy that was feasible in view of the successful transition to adulthood of targeted infant industries that had been promoted in the previous decade. This also led to a massive restructuring of exports. The cornerstone of the continued strategy of export-led development was the maintenance of a high degree of international competitiveness.

The second-tier NIEs – Indonesia, Malaysia and Thailand – also undertook a large-scale liberalization of their trade regimes and completed their transition from ISI to export-led development policies. This again was feasible because of the relative efficiency of industries that had been promoted earlier in a targeted and coherent ISI regime. These countries also liberalized their investment policies, a reform that encouraged large inflows of foreign direct investment (FDI). The structure of exports was radically altered in the process of greater integration into the world economy and was facilitated by the maintenance of a high degree of international competitiveness.

By the mid 1980s China was also making a decisive transition to export-led growth by sharply shifting incentives in favour of exports while retaining many of the controls over and regulations governing trade and industry. Among the policies that had a major role in this transition were adjustments to the exchange rate, numerous forms of targeted support to export industries and vast liberalization of foreign investment.

Reforms in the Philippines during the 1980s were less effective. Its industries, developed under an indiscriminate ISI regime and suffering from a lack of competition, were not subjected to radical reform and the trade regime continued to discriminate against exports. A combination of political instability, ineffective attempts to stabilize the macroeconomic imbalance and failure to ensure international competitiveness led to a loss of the Philippines' share of the world export market and delayed its access to the benefits of the world economy until the early 1990s.

GROWTH AND INTEGRATION DURING THE 1980s AND 1990s

Integration into the Global Economy

This section considers how well the ESEA countries have succeeded in taking advantage of the increased globalization of the world economy since the beginning of the 1980s and the extent to which their increased integration into the world economy has contributed to their growth. Between 1981 and 1993 ESEA exports grew at an average annual rate of 11.2 per cent, compared with 5.3 per cent for the LDCs as a whole¹⁰ and 5.4 per cent for the world as a whole (World Bank, 1996a, p. 80). During this period the ESEA share of FDI also increased rapidly. In 1994 it attracted 54 per cent of the FDI received by all LDCs (*ibid.* p. 84).

Tables 5.4, 5.5 and 5.6 highlight some of the features of the accelerated integration of the ESEA countries into the global economy. As seen in Table 5.4, of the first-tier NIEs, Korea continued to show an increase in its export/GDP ratio between 1980 and 1994 but Taiwan experienced a fall in this ratio. As already noted, Taiwan's export/GDP ratio in 1980 was unusually high. Indeed the annual growth rate of Taiwan's exports was well over twice the growth rate of world exports. The exports of the second-tier NIEs increased extremely rapidly, especially during the early 1990s. China's exports increased at a dramatic rate: between 1980 and 1994 China's export/GDP ratio quadrupled! The Philippines was the only country to experience slower export growth than the rest of the world, and it was only in the early 1990s that its exports began to grow rapidly.¹¹

A second important feature of export growth is an increase in the share of manufactured exports and a fall in the share of primary exports. The first-tier NIEs already had a high ratio of manufactured exports to total exports at the beginning of the 1980s, the period of accelerated globalization, and since then there has been a further increase in the ratio. The change in the ratio of manufactured exports to total exports hides the remarkable change in the composition of manufactured exports that took place in the first-tier NIEs during this period. To illustrate, machinery and transport equipment as a proportion of total exports increased in Korea from 20.3 per cent in 1980 to 42.3 per cent in 1993, and in Taiwan from 24.7 per cent in 1980 to 44.2 per cent in 1993 (Table 5.4).

The second-tier NIEs have experienced a dramatic change in the composition of their exports in favour of manufactured goods, particularly the more sophisticated products. Exports of machinery and transport equipment as a proportion of total exports increased from 11.5 per cent in 1980 to 40.5 per cent in 1992 in Malaysia, and from nearly 6 per cent to over 27 per cent in Thailand (Table 5.4). The composition of China's exports has similarly changed: not only did manufactured exports rise sharply as a proportion of

Table 5.4 Growth and composition of exports from East and South-East Asia¹

	<i>Exports/GDP ratio</i>		<i>Growth rate of exports (% p.a.)</i>		<i>Manufactured exports as % of total exports</i>		<i>Machinery exports as % of total exports</i>	
	1980	1994	1980-90	1990-94	1980	1993	1980	1993
Korea	34	36	13.7	7.4	90	93	20.3	42.3
Taiwan	48 ²	38 ²	13.1	8.0	88	96	24.7	44.2
Indonesia	24	34	5.3	21.3	3	48	0.5	4.5
Malaysia	58	90	11.5	17.8	19	65 ³	11.5	40.5 ³
Thailand	24	39	14.3	21.6	28	73	5.9	27.7
China	6	24	11.4	14.3	48	81	2.9	15.9
Philippines	24	34	2.9	10.2	37	76	2.1	18.7

Notes

1. Exports refer to exports of goods and non-factor services in the first two columns (except for Taiwan) and to merchandise exports only in the other columns. Growth rates are based on values at constant price, that is, current price values deflated by the relevant price indices.
2. Merchandise exports only.
3. 1992.

Sources: Taiwanese data from ADB (1993, 1996); China, SSB (1996); Data for manufactured exports and machinery exports are from World Bank (1993d); All other data are from World Bank (1996a).

total exports, between 1980 and 1995 machinery and transport equipment as a proportion of total exports increased from 4.7 per cent to 21.1 per cent (China, SSB, 1996, p. 581). The Philippines have also experienced a substantial diversification of exports, although there are important qualifications to the significance of this. Technologically advanced manufactured exports largely represent low-value-added activities carried out in export-processing zones that use a large proportion of imported inputs and have very limited linkage to the rest of the economy (Khan, 1997).

A third notable feature of export growth of the ESEA countries is a rise in the share of exports to other LDCs, especially those in Asia, and declining dependence on the OECD market for export growth (Table 5.5). Thailand and the Philippines are the only exceptions to this trend. In future the OECD countries are likely to grow at a much slower rate than the LDCs, especially the Asian LDCs, which are likely to continue to be in the front rank of rapidly growing economies. A shift of exports away from the OECD countries with slow growth in demand and towards faster growing economies will be favourable to the ESEA countries. This particular outcome is also directly related to policy reform in these and other LDCs during the period of globalization. In the past, these countries, with the exception of the first-tier NIEs, often allowed their domestic currencies to be artificially overvalued, a practice that

Table 5.5 Direction of trade of East and South-East Asia (percentage of exports of countries of origin)

Country of origin	Destination					
	Asian LDCs		OECD		Other	
	1985	1992	1985	1992	1985	1992
Korea	12.9	25.4	62.3	53.1	24.7	21.5
Taiwan	15.6	28.4	34.7	—	49.7	—
Indonesia	17.2	24.4	75.1	63.5	7.6	12.1
Malaysia	38.1	41.1	52.9	47.9	9.1	11.1
Thailand	27.1	21.9	52.8	59.9	20.2	18.1
China	38.2	53.5	39.4	32.9	22.5	13.6
Philippines	19.5	12.9	70.8	81.8	9.7	5.4

Source: ADB (1994).

Table 5.6 Indices of real effective exchange rates in East and South-East Asia (1985=100)

	1988	1990	1993
Korea	93.6	107.3	99.9
Taiwan	100.3	106.8	94.7
Indonesia	55.5	54.4	54.6
Malaysia	71.7	66.7	77.3
Thailand	79.3	83.5	78.9
China	79.9	68.0	73.8
Philippines	74.5	76.3	77.8

Source: ADB (1994).

made their exports to each other unattractive relative to exports from the OECD countries. As Table 5.6 shows, most of these countries have sharply reduced the value of their currencies in real terms since the middle of the 1980s.

As for FDI, while the ESEA countries as a group have attracted a very large and increasing share of total FDI going to all LDCs, the pattern has been vastly different among individual countries. The principal advantage of FDI is that, in addition to augmenting investable resources, it provides access to technology, management expertise and the international market. Korea and Taiwan were neither hospitable towards nor dependent on FDI during their early development. This pattern continued for Korea and was only moderately relaxed in Taiwan during the period of accelerated globalization. Their domestic savings rates were high enough for them not to depend on foreign capital. Korea preferred to acquire technological knowledge through licensing arrangements, while in recent years Taiwan has been more disposed towards direct participation by transnational corporations in selected industries.

FDI as a proportion of investment has generally been higher in the second-tier NIEs. The ratio has been particularly high for Malaysia (Table 5.7), although the most dramatic increase in FDI has taken place in China in recent years. In 1994 China accounted for 42 per cent of all FDI going to LDCs! None of the second-tier countries had a pressing need for FDI as a source of augmenting investable resources, rather the main reason for seeking FDI was to gain access to technology, management skills and the international market.

A major determinant of the success of the ESEA-6 in taking advantage of the globalizing world economy was their ability to maintain a high degree of international competitiveness by stabilizing the unit labour cost in foreign exchange, in spite of increasing real wages. This was achieved through the combination of a rapid increase in labour productivity, a low rate of domestic inflation relative to world inflation and adjustment to the exchange rate.¹² Labour productivity increased rapidly due to the emphasis placed by these countries on human capital investment and the overall incentive structure that guided investment towards socially profitable activities. Both groups of NIEs achieved substantially lower rates of inflation during the 1980s and 1990s than in the preceding decade (Table 5.8). China's inflation was higher during the 1980s and 1990s than previously; but the aggressive adjustment in the exchange rate allowed China to stabilise its unit labour cost in foreign exchange. The Philippines failed to stabilize its unit labour cost in foreign exchange because of its inability to improve labour productivity and to contain the rate of inflation.¹³

These countries were not only competing against others in the international market, they were also competing against each other. What prevented this

Table 5.7 Foreign direct investment as proportion of investment in East and South-East Asia¹

	1981-85	1986-90	1994
Korea	0.5	1.3	0.6
Taiwan	1.5	3.5	2.4 ²
Indonesia	1.0	2.0	4.2
Malaysia	10.8	10.5	16.3
Thailand	3.2	5.9	1.2
China	n.a.	n.a.	15.5
Philippines	n.a.	n.a.	6.5

Notes:

1. Data for 1981-85, 1986-90 and 1993 (Taiwan) are FDI as a percentage of gross fixed capital formation. For 1994 the figures refer to the ratio of FDI to gross investment.
2. For 1993.

Sources: UNCTAD *World Investment Report* (various years); World Bank (1996a, 1996b).

Table 5.8 Annual rates of increase in the consumer price index in East and South-East Asia

	1971-80	1981-90	1991-93
Korea	16.5	6.4	7.1
Taiwan	11.1	3.1	3.6
Indonesia	17.5	8.6	8.6
Malaysia	6.0	3.2	4.3
Thailand	10.0	4.4	4.3
China	1.1	7.5	9.4
Philippines	14.8	13.0	11.7

Source: ADB (1994).

from becoming a 'beggar-thy-neighbour' game was the fact that the individual countries restructured their production and exports according to the changing pattern of comparative advantage.

Economic Growth

The six ESEA countries that successfully integrated into the global economy all attained high growth in GDP during the period of economic globalization (Table 5.1). The Philippines, which failed to take advantage of the increased globalization, stagnated during the 1980s and its performance only began to improve in 1994.

During the 1980s Korea maintained an annual GDP growth rate that was almost as high as during the preceding decade. Taiwan's growth rate during the 1980s was significantly lower than in the previous decade, though still very high by international standards. During the early 1990s the growth rate of both these countries fell further, though remaining 3.6 times the world average! As noted earlier, for years Taiwan has had a per capita income that almost puts it in the World Bank's high-income-country classification. It is currently at top of the league of the upper-middle-income countries and is destined to be the next country to enter the top rank. However, while Korea and Taiwan have enjoyed unprecedented development achievements in many areas in the past, it is unlikely that their economies will continue to grow at their historical rates. Nonetheless their growth performance in the period of globalization must be regarded as remarkable by any standard.

Among the second-tier NIEs, Thailand experienced steady acceleration of GDP growth during the period of globalization. Its annual population growth rate is now down to 1 per cent and per capita income has been growing by more than 7 per cent a year. The GDP growth rates of Indonesia and Malaysia declined somewhat in the early to mid 1980s due to the short-term

retrenchment effects of stabilization, but since then they have accelerated steadily.

China's growth performance during the era of globalization has been historically unprecedented. Never before has more than a fifth of humankind experienced a more than 10 per cent increase in GDP (about 9 per cent in per capita GDP), sustained over a decade and a half.¹⁴

The Philippines is the only ESEA country in our list not to conform to this pattern of high growth. In fact, during the period of globalization it experienced negative growth in per capita income and its per capita GDP was lower in 1995 than in the early 1980s.

The remarkable growth performance of the ESEA-6 during the period of globalization was the result of development strategies that cannot be analysed adequately in the present study. One might characterize them as extensions of the strategies used in the 1960s and 1970s, briefly outlined in the first section, with modifications necessitated by increased integration into the global economy. These modifications were efficiency augmenting: for the second-tier NIEs and China in particular, outward-looking reforms led to more efficient resource use. As the incentive to save and invest was kept as high as before, and targeted support to worthwhile industries remained intact, this led to high growth.

Information Technology

Globalization has been facilitated by the rapid spread of information technology. Activities that encompass the electronics industry, telecommunications and information services, including computers, semiconductors, software and information systems, have reduced the cost of international communication and facilitated the flow of information. IT has therefore emerged as a critically important factor in the accelerated process of economic globalization.

A recent World Bank study of the role of IT in the development of East Asia identifies three distinct aspects of its importance.¹⁵ First, it is an industry whose output demand is highly income elastic and rapidly growing. If a country can obtain comparative advantage in some aspect of the industry, this is a very important source of export revenue. Second, IT makes an important contribution to increased industrial productivity by enhancing the efficiency of both management and technology. Third, IT can contribute to overall economic efficiency through modernization of the transport and communication infrastructure.

An important point about IT activities is that comparative advantage in some segment of it is feasible for countries with vastly different factor endowments and most of its components are 'footloose'. Some processes (for example the assembly of microelectronics and computer motherboards) can

be undertaken in countries with abundant unskilled and semi-skilled labour, as happens in Malaysia and the Philippines; while other processes require more sophisticated skills, such as those available in Korea and Taiwan.

The appropriateness of using IT for the enhancement of production technology of course varies from one country to another depending on whether it is complementary to or competitive with other production factors. It is conceivable that certain IT-based production techniques will replace labour and hence be inappropriate for a labour-abundant LDC (for example Indonesia) but quite appropriate for an LDC that is well on its way towards comparative labour scarcity (as Korea and Taiwan appear to be).

Information on different aspects of IT adoption in LDCs is often not readily available. The evidence that is available suggests that the ESEA countries are among the foremost LDCs in terms of carving out a market share in the IT industry. In 1993 Korea and Malaysia respectively had 9.5 per cent and 7.5 per cent of the world export market in electronic microcircuits, 4.7 per cent and 8.6 per cent of the market for diodes and transistors, and 6.1 per cent and 2.6 per cent of the market for automatic data processing (ADP) peripherals. Korea had 3.1 per cent of the market for digital computers. Singapore and Hong Kong, the high-income ESEA economies, had large shares of the world market in these IT products. Thailand, China and the Philippines had also entered the world export market in IT products. Together all these ESEA countries had 31.4 per cent of the world export market in electronic microcircuits, 27.7 per cent of the market in diodes and transistors, 38.8 per cent of the market in ADP peripherals and 28.4 per cent of the market in digital computers.¹⁶ Information is not available about Taiwan's share. Clearly the ESEA region had become the largest country group, outside the OECD, to produce and export IT products.

Table 5.9 summarizes the available information on some indicators of the extent of use of IT in four of the ESEA countries in 1989. Korea had clearly attained a high level of IT use by LDC standards and was already on the way to the level of use in some OECD countries. Taiwan may also have attained a comparable stage of development, although information is not readily available in this regard. The other ESEA countries were still at a comparatively low level of use of IT.

Within ESEA the strategy for IT development varies among countries. The Korean strategy is probably representative of that of the first-tier NIEs. In 1992 Korea adopted an IT master plan, which set the following targets: an increase of personal computers and terminals from 2.2 million to 10 million by 2001; an increase in the share of locally produced computers from 3 per cent to 50 per cent; development of 256-Mbit DRAM chips within three to four years; development of broad-band information service digital networks for cellular phones; and establishment of a centre to map out a standard linking code in Korean and other languages (Hanna *et al.*, 1996, p. 87). The

strategy adopted for the achievement of these targets was similar to that used in the past for the development of industries, namely broad-range but targeted public support. The IT industry has been protected from competition from established producers abroad. However, it has been recognized that the domestic market is not sufficiently large to allow the efficient development of the industry. Thus the protection afforded is not inward-looking; support is extended to enable them to expand exports as well. Government procurement is used to guarantee a minimum market. R&D support from the public sector amounted to 64 per cent of total R&D in the industry in 1980, falling to 20 per cent in the early 1990s. The use of IT in government administration was promoted to encourage the expansion of domestic demand. Providing R&D tax incentives to the private sector, encouraging industries to automate and investing in the human capital required for R&D development are other measures that helped the development of the IT industry.¹⁷

In stark contrast to this comprehensive strategy of developing IT and using it to enhance productivity and efficiency throughout the economy, is the case of the semiconductor industry in the Philippines. In 1987 imported inputs amounted to 76.3 per cent of the value of exports of the IT industry. While the industry accounted for 10.2 per cent of exports, it contributed only 0.4 per cent of value added and 0.14 per cent of employment to the economy.¹⁸ The low linkage between this industry and the rest of the economy was due to its development in enclaves under the auspices of FDI, attracted by incentives that were strong enough to induce their location in the country but insufficiently strong to promote their integration into the rest of the economy. While this development has brought other important benefits to the Philippines, semiconductor exports have contributed little to the economy.

Table 5.9 Indicators of information technology for East and South-East Asia, 1989

	<i>Korea</i>	<i>Thailand</i>	<i>Malaysia</i>	<i>Philippines</i>	<i>Brazil</i>	<i>USA</i>
Telephone lines per thousand persons	28.32	2.08	7.35	0.95	6.00	50.58
Per capita sale of telecom services (\$)	92.87	14.53	33.54	8.44	8.40	442.35
Mainframe computers per million persons	222	n.a.	n.a.	n.a.	n.a.	8287
Per capita sale of data processing (\$)	10.70	0.71	3.63	0.43	1.61	39.06
Per capita sale of information processing services (\$)	9.40	n.a.	n.a.	n.a.	n.a.	414.00

Source: Hanna *et al.* (1996).

Malaysia perhaps represents an intermediate case in which the IT industry has been promoted by FDI but has been more successful in creating linkages between this industry and the domestic economy by encouraging a more rapid diffusion of IT use. Unfortunately there is insufficient information available to analyse this comprehensively.

TRENDS IN POVERTY

This section aims to determine the trends in the incidence of poverty in the ESEA countries during the 1980s and 1990s, the period associated with accelerated globalization. As shown below, poverty reduction has been less uniform among the ESEA countries than their growth performance.

Poverty is measured by the number of the population below some threshold per capita income or expenditure that is held constant over time. Such thresholds do not represent constant standards of living across countries. Although the thresholds are frequently anchored to a minimum acceptable level of nutrition, as indicators of the living standard they differ between countries for a variety of reasons, for example differences in the nutritional standards used between countries, intercountry differences in consumption patterns, and differences in the method of allowing for non-food needs when estimating the poverty threshold. Thus the levels of absolute poverty are not comparable between countries. Furthermore it is not clear that use of a uniform poverty threshold for all countries, had it been possible to do so, would have changed the findings.

The First-Tier NIEs

Korea and Taiwan are among the countries with the most egalitarian distribution of income and a low incidence of absolute poverty. Indeed the incidence of poverty, by any reasonable standard, had declined to very low levels in Korea and Taiwan by the early 1980s and there is little evidence that high growth in the period of globalization has been associated with increased inequality. For Korea the Gini ratio of income distribution is estimated to have declined from 0.389 in 1980 to 0.345 in 1985 and 0.336 in 1988 (Korea Labor Institute, 1992, p.126). The hourly real wage in industries increased at an annual rate of 9.3 per cent from 1982–90 (*ibid.*, p. 65). Direct estimates of change in the distribution of income are not readily available for Taiwan, but real manufacturing earnings increased at an annual rate of 4.4 per cent between 1979 and 1985 and 9.4 per cent between 1985 and 1990 (ADB, 1994, p. 207). The unemployment rate in both these countries declined between 1985 and 1990 (*ibid.*). Although direct estimates are not available,

it is almost certain that the incidence of absolute poverty, according to any reasonable criteria, has fallen in these countries.

The Second-Tier NIEs

Tables 5.10, 5.11 and 5.12 provide estimates of the trends in poverty in Indonesia, Malaysia and Thailand during the 1980s and early 1990s. The incidence of poverty in all these countries declined over this period although the extent and pattern of poverty reduction varied.

In Indonesia the incidence of poverty in both rural and urban areas declined steadily throughout the period under review. A notable feature of the trend is that between 1981 and 1987 – the period of stabilization and decline in GDP growth rate – poverty reduction took place at a faster rate than during the subsequent period of faster growth and more rapid integration into the global economy.

Successful reduction of poverty during the stabilization period was due to the fact that fiscal retrenchment concentrated on the capital-intensive sectors and government programmes had little adverse effect on employment growth. In addition the severity of retrenchment was limited due to the cooperation of donors and creditors, who allowed a continued inflow of net resources. In more recent years the fall in the rate of poverty reduction has been attributed to the isolation of the remaining poor in remote pockets of poverty that are not easily reached by public programmes.

The incidence of poverty in Malaysia has declined more rapidly than in the other NIEs. By the early 1990s poverty in urban Malaysia had become insignificant and poverty in rural areas had been reduced to a very low level. Poverty reduction during the early to mid 1980s – the period of stabilization

Table 5.10 Trend in poverty incidence in Indonesia
(percentage of population below the poverty threshold)

	<i>Rural</i>	<i>Urban</i>
1980	28.4	29.0
1981	26.5	28.1
1984	21.2	23.1
1987	16.4	20.1
1990	14.3	16.8
1993	13.1	14.2

Note: These are estimates by the Central Bureau of Statistics. Poverty threshold refers to per capita expenditure based on the cost of 2100 kilocalories of food energy and a further mark up for non-food expenditure.

Table 5.11 Trend in poverty incidence in Malaysia
(percentage of population below the poverty threshold)

	<i>Rural</i>	<i>Urban</i>
1973	55.3	22.9
1984	27.6	6.5
1987	24.7	7.3
1989	13.0	2.2
1995	6.5	1.9

Note: Poverty threshold refers to RM33 per capita per month at 1970 prices, using the consumer price index in subsequent years.

Source: Samudram (1996).

Table 5.12 Trend in poverty incidence in Thailand
(percentage of population below the poverty threshold)

	<i>Whole country</i>	<i>Villages</i>
1981	23.0	27.3
1986	29.5	35.8
1988	22.8	26.3
1992	18.6	20.7

Note: Poverty threshold refers to an income level that provides adequate nutrition (along with other basic necessities).

Sources: Suganya and Somchai (1988); Medhi *et al.* (1992); Medhi (1996).

and reduced growth – was due to an improvement in income distribution. Accelerated growth from the late 1980s was not accompanied by a significant worsening of the distribution of income, so that the pace of poverty reduction was maintained.¹⁹

In Thailand the incidence of poverty increased during the period of increased globalization and declined thereafter. Over the period as a whole there was a substantial reduction in poverty, although some of the potential poverty-reducing effects of the sharp acceleration in growth were offset by increased inequality in the distribution of income. A recent study by Medhi (1996) reports that from 1988–90 about 36 per cent of the reduction in the headcount index of poverty that would have resulted from income growth, with unchanged distribution, was offset by the adverse change in income distribution. The same study reports simulation exercises that show that the radical reduction in effective protection in the late 1980s – directly deriving

from Thailand's greater integration into the world economy – contributed to poverty reduction. Higher growth in the period of globalization also helped channel more resources into poverty-alleviating programmes. Since the mid 1980s the share of economic and social services in total public expenditure has increased rapidly, with a favourable impact on the poor.

China²⁰

China embarked on a massive reform of the rural economy in 1979 and until the mid 1980s its remarkable growth was largely led by the growth of the rural economy. From the mid 1980s the focus of China's development strategy shifted away from the rural economy in favour of export-led growth, whereby the Chinese economy became rapidly integrated into the global economy.

There was a sharp decline in the incidence of poverty in rural China until the mid 1980s, but thereafter the rate of decline slowed dramatically and in the early 1990s it ground to a complete halt (Table 5.13), with a consequent rise in the absolute number in poverty. In urban China there was a steady fall in the incidence of poverty until the end of the 1980s, but in the 1990s this trend reversed. Overall China's poverty-reduction record during the period of increased integration into the global economy was poor, in sharp contrast to its remarkable growth performance during the same period.

The asymmetrical performance in poverty reduction in the pre-1985 and post-1985 period in rural China is largely explained by a fall in the growth rate of *personal* income (the variable that features in the poverty threshold).

Table 5.13 Trend in poverty incidence in China
(percentage of population below the poverty threshold)

	Rural		Urban	
	Standard PIT	Low PIT	Standard PIT	Low PIT
1980	59.8	40.8	n.a.	n.a.
1981	48.3	30.3	44.3	20.1
1983	26.4	14.3	n.a.	n.a.
1985	24.5	14.0	26.2	12.7
1988	27.0	16.1	n.a.	n.a.
1989	n.a.	n.a.	17.7	7.4
1990	23.9	13.9	15.0	7.4
1991	n.a.	n.a.	12.2	4.7
1992	22.9	13.6	n.a.	n.a.
1993	23.7	14.1	n.a.	n.a.
1994	23.1	13.6	12.0	5.9

Note: PIT stands for poverty income threshold.

Source: Khan (1996c).

In the earlier period, personal income grew rapidly due to a high rate of growth of agricultural output and a sharp improvement in the agricultural terms of trade. The effect of growth was strong enough to outweigh the effect of moderately rising inequality in the distribution of personal income. In the later period the rate of growth of personal income declined drastically due to a fall in agricultural output and a decline in or stagnation of the agricultural terms of trade. The growth in personal income was no longer high enough to offset the effect of inequality, which continued to rise. Since most of China's poor are located in rural areas, the decline in the rate of rural poverty reduction affected China's overall poverty-reduction statistics.

Until the late 1980s the rate of growth of personal income in urban China was high enough to outweigh the effect of the moderate rise in inequality. Thereafter growth in personal income accelerated, but it could no longer outweigh the effect of what was now a sharp increase in the inequality of income distribution.

An important point emerging in the case of China is that the overall growth rate of GDP is a poor predictor of the growth rate of personal income, the variable that features in the estimation of poverty. This is due partly to macroeconomic policies concerning the rate of accumulation, and partly to a change in the sectoral terms of trade, which feature prominently in the transmission of aggregate growth to sectoral growth.

The unprecedented rate of industrialization in the era of China's integration into the global economy (1984–94) contributed to income concentration in two very important ways. First, the output elasticity of employment in manufacturing fell drastically, from 0.62 in 1978–84 to 0.27 in 1984–94. This was in spite of the fact that the growth in manufactured exports was mainly in labour-intensive products. The explanation of this paradox seems to lie in the initial condition of the manufacturing industries, mainly state and collective enterprises: in the past employment had been expanded beyond the dictates of efficiency as part of the social policy of guaranteed employment. Economic reforms aimed at integration into the world economy made it increasingly difficult to continue this system of social protection. Both state and collective enterprises, in their quest for greater efficiency and collaboration with foreign investors, began to shed surplus labour during the period of globalization and this process gained momentum once legal cover was gradually extended to it. The observed low output elasticity of employment was the sum of two divergent effects: (1) a fairly high output elasticity of employment measured at constant intensity of employment per worker; and (2) a rise in the intensity of employment due to a reduction of concealed unemployment in industry. The process was certainly efficiency enhancing and one could argue that its adverse distributional impact might have been mitigated by appropriate social policies, for example unemployment insurance and/or an accelerated public works programme. Second, growth was concentrated in the richer coastal and

eastern provinces, regions that attracted the most FDI. These trends were closely related to the fact that reforms aimed at facilitating the integration of China into the world economy were not offset by policies to protect the unemployed and the poorer regions.

Some specific aspects of development policy deserve to be highlighted in connection with the disequalizing effects that were unleashed by China's greater integration into the global economy. The push for an ever higher rate of accumulation was an obstacle to the growth of GDP being transformed into growth of personal income. The change in the composition of public expenditure and credit away from the rural sector and towards the urban sectors of the richer provinces was detrimental to overall poverty alleviation. The policy of allowing the state and collective enterprises to shed underemployed labour was not matched by an adequate policy to protect the unemployed. While the official tolerance of migration should have benefited the poor, *de facto* discrimination against them has impeded their welfare.²¹ Institutional changes to the provision of education and health services were not complemented by increased public funds that would allow the poor to gain access to these services.²²

The Philippines

Because of its dismal growth performance until the early 1990s the Philippines is an unlikely country to have experienced a reduction in poverty. It is therefore surprising that the incidence of poverty declined, albeit slightly, between 1985 and 1991 (Table 5.14). With the resumption of growth in 1994 there was more of an impetus for poverty reduction in urban areas. The relationship between growth, inequality and poverty has been different in different periods. From 1985–88 real per capita GDP increased by 12 per cent. According to the Family Income and Expenditure Survey (1985, 1988, 1991) real consumption per capita was stagnant, indicating a failure to convert growth of aggregate GDP into improved living standards. The incidence of poverty nevertheless declined due to an improvement in the distribution of expenditure in rural areas. From 1988–91 there was almost no growth in per capita GDP and inequality in distribution increased. The result was an increase in the incidence of poverty.

Greater integration into the global economy, prompting a downward adjustment of the exchange rate, appears to have contributed to increased poverty in the Philippines. According to Balisacan (1996) a 5 per cent devaluation increases the rural headcount ratio of poverty by 1.9 percentage points and the urban headcount ratio by 2.5 percentage points. Since agricultural products are more tradable than those of industry in the Philippines, the devaluation substantially raised rural prices. The resulting terms of trade improvement did not benefit the rural poor, who are largely landless workers

Table 5.14 Trend in poverty incidence in the Philippines
(percentage of population below the poverty threshold)

	<i>Rural</i>	<i>Urban</i>
1985	56.4	37.9
1988	52.3	34.3
1991	55.1	35.6
1994	53.7	28.8

Note: Poverty threshold is the one officially estimated by the Inter-agency Technical Working Group on Poverty Determination and is believed to be relatively high compared with the ones for Indonesia and Thailand.

Source: Balisacan (1996).

and small farmers, net buyers of food. The urban poor also faced a higher increase in food prices than in nominal earnings.

CONCLUSIONS

During the 1980s and early 1990s the ESEA-6 achieved a greater degree of integration into the global economy by increasing their share of world exports and FDI. The success of both tiers of NIEs in this task was strongly facilitated by the relative efficiency of the industries that their past development policies had promoted. This enabled them to compete internationally in a more liberalized trading system. Their ability to maintain international competitiveness was another critical element in ensuring their successful integration into the global economy.

The period of globalization also witnessed a high rate of growth for these economies as they maintained the positive elements of their past development policies and reinforced them further by the efficiency-enhancing reforms that were introduced as part of their programme of increased integration into the global economy. Strong emphasis on the IT industry, especially in the first-tier NIEs, was another important element of increased integration and higher growth. Their growth in the period of globalization was not associated with a significant increase in inequality of income distribution. As a consequence they all experienced a continued reduction in the incidence of poverty.

China's remarkable success in increasing its share of global trade and FDI was due to a sharp shift in its development policy towards exports and international competitiveness. The resulting improvement in the efficiency of resource use, combined with continuation of the high investment rate, led to a very high rate of growth in GDP. However, the process unleashed

strongly disequalizing forces, which led to an increase in inequality and a halt to the reduction of poverty that China had experienced before its integration into the global economy.

The Philippines failed to take advantage of the process of globalization due to its inability to maintain international competitiveness and its failure to break out of the inefficient ISI regime sufficiently quickly. Political instability and the absence of a coherent development strategy led to a decline in the rate of investment and the prolonged stagnation of GDP, from which it has only recently started to recover.

It is useful to note that specific elements of globalization can have asymmetrical redistributive effects under different circumstances. Trade liberalization and exchange rate adjustment seem to have improved the distribution of income in Thailand but adversely affected the poor in the Philippines. It is also important to exercise caution in attributing the absence of favourable distributional trends in China and the Philippines during the period of globalization to these countries' increased integration into the world economy. In the case of China, the adverse distributional effects are transitional and due to the initial distortion of its industries. This could have been offset by compensatory policies during the transition period.²³ In the Philippines the main cause of persistent poverty is slow growth. Greater integration into the global economy would almost certainly have contributed to higher growth in the Philippines.

Notes

1. This chapter employs the same notion of globalization as Chapter 4 on South Asia. As is stated in that chapter, the world economy has been gradually moving towards greater integration for a long time, but the process accelerated at the beginning of the 1980s. What is often referred to as the 'period of globalization' in this chapter should more accurately be called, as indeed it is from time to time, 'the on-going period of accelerated globalization of the world economy'. This longer phrase is often replaced by the shorter one in the interest of brevity.
2. As will be discussed later, their outward-looking strategy did not mean that they rejected protection in favour of free trade. It was outward looking in the sense that there was an absence of discrimination against exports. In the promotion of targeted industries there was no discrimination in favour of industries that sold their products in the domestic market relative to industries that sold their products abroad.
3. The World Bank classifies these two territories as high-income countries (HICs). According to World Bank (1996a), the per capita GNPs of these territories are close to or above that of the median of the 25 HICs that have at least one million people each. Indeed Taiwan would be included in the group of HICs, according to the World Bank classification, if it were recognized as a country, though it would rank second last in the group. Its per capita income in 1994 was 54 per cent

- of that of Hong Kong and 52 per cent of that of Singapore. Note that the United Nations includes Hong Kong and Singapore in the category of 'developing countries', a classification with which the authorities in these countries seem to agree.
4. There is no unanimity of view as to whether Myanmar should be designated as part of South Asia or South-East Asia. Even if one were to consider it part of South-East Asia, it would not make sense to include it in the present study because of the absence of relevant information and because of its long-term adherence to autarkic policies from which it is only now beginning to emerge. The ESEA region in this chapter excludes the Pacific Islands (including Papua New Guinea).
 5. According to the IMF (1996, p.123).
 6. As shown later, Taiwan was the only country in this group to experience a reduction in the ratio of exports to GDP during the period of globalization. All the others succeeded in increasing their export/GDP ratios. The reduction in Taiwan's export GDP ratio started from a very high base and the ratio has remained very high in recent years.
 7. The primary school enrolment rates were 67 per cent for South Asia and 68 per cent for North Africa and the Middle East. For Latin America, which was considerably richer at the time, it was 95 per cent. All these data are from World Bank (1995a).
 8. For various interpretations of this experience see Amsden (1979), Wade (1990, 1996) and World Bank (1993b).
 9. See Khan (1997) for an account of the Philippines experience.
 10. Estimates of the export growth of the non-ESEA LDCs are not available, but growth was clearly much lower.
 11. For an account of the poor performance of the Philippines in this and other regards see Khan (1997).
 12. The underlying analytical model and the evidence for Korea and Malaysia can be found in Mazumdar (1993). Evidence for China is provided in Khan (1996d).
 13. This is documented in Khan (1997).
 14. Admittedly, as shown in the next section, this average growth was not shared equally by all the 1.2 billion people of China.
 15. See Hanna *et al.* (1996). The report provides case studies of IT in Japan, Korea, Taiwan, Hong Kong and Singapore.
 16. This information is from Chapter 2 of this volume.
 17. See Hanna *et al.* (1996, pp. 90–2) for an account of the Korean strategy.
 18. See Krugman *et al.* (1992, p.12) for this information. Unfortunately more recent information is not available.
 19. See Samudram (1996) for some of the evidence.
 20. The analysis of poverty trends in China is based on Khan (1996c), which provides detailed evidence that can not be reproduced here for reasons of space.
 21. There has been a very large flow of migrants out of rural areas into cities, where in the past migration was controlled by the strict enforcement of residence permits. This enforcement has been relaxed, but the migrants have not been granted access to public resources such as subsidized education, health services and housing.
 22. In the past these services were provided by collective institutions. The dismantling of these institutions has not been followed by adequate provision of services by local government or other bodies.
 23. Admittedly these compensatory policies might have affected the pattern of globalization. It is possible that a policy of greater regional balance in public

investment would have affected the volume and pattern of FDI. Similarly a policy of greater social protection might have reduced the rate of accumulation and growth.