University of Wisconsin-Madison
Department of Agricultural & Applied Economics

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Southeast Asia's Long Transition

By

Ian Coxhead

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Ian Coxhead, University of Wisconsin-Madison

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Abstract

Southeast Asia's 620m people are experiencing a remarkable transition from widespread poverty to comparative wealth. The region's long-run GDP growth rate is second only to that of East Asia, far ahead of average rates for other developing regions. This rate of economic expansion has been sustained in spite of internal shocks and global market volatility. Tens of millions have been lifted out of poverty as a result. This impressive record contradicts pessimistic predictions from many global growth models. Is Southeast Asia different, and if so in what ways?

In the early 21st century the region is undergoing broad and deep regional and global integration with relatively stable macroeconomic conditions. Nevertheless, numerous old problems remain, and new issues have arisen. Sustaining growth and reducing vulnerability to shocks remains a daunting challenge for the future.

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1. Introduction

As of 2014 Southeast Asia is home to 620m people, or 8.6% of world population. Its six large economies (Indonesia, Singapore, Thailand, Malaysia, the Philippines and Vietnam) and five smaller ones (Cambodia, Laos, Myanmar, Brunei and East Timor) together account for one-tenth of the income generated in all low and middle-income economies worldwide. Less than two generations ago the vast majority of Southeast Asians were very poor. Since the 1980s, however, the region as a whole has achieved and sustained a remarkable rate of growth (Figure 1), in the course of which tens of millions of its citizens have successfully escaped severe poverty. This growth experience sets the region as a whole apart from other developing areas (only China can claim a consistently higher growth rate of per capita GDP) and has seen incomes in most Southeast Asian countries lifted well above the developing-country average (Figure 2).

Figure 1 about here

Figure 2 about here

Despite this remarkably convergent growth, however, the countries of the region display a great variety of development experiences. This is due in large part to differences in initial resource endowments, systems of government and development strategies, and the pace and extent of their integration with external markets. Today's high degree of international market integration in the region is a phenomenon with deep roots in the region's historical role both as a unique supplier of spices and other natural resource products, and as an entrepôt on maritime trade routes linking the world's largest economies. In recent decades, Southeast Asia's outward orientation has been reinforced by adoption of growth and development strategies that exploit trade-based opportunities created by its abundance of labor and natural resources and by its geographic, cultural and economic proximity to large, fast-growing economies in Northeast Asia. Countries of the region (Myanmar excepted) display high and/or rising trade intensity relative to the world average (Figure 3). The nature of Southeast Asia's contemporary economic development experience is increasingly dominated by its ever-closer integration into the wider Asian and global production and trade networks for agriculture, resources, manufactures—and increasingly, of services.

Figure 3 about here

Another striking feature of the region's recent development is the pace and extent of transformation of production and sources of household income. Fifty years ago, nearly all inhabitants of this region lived in rural areas and relied their own labor to supply food, shelter and other necessities of life. But in less than three decades from the early 1970s, the region's economic center of gravity moved from primary industries (agriculture, fisheries, mining and forestry) to manufacturing—initially, raw materials processing and simple assembly operations, but becoming more technologically sophisticated over time (Figure 4). This sectoral transformation occurred at a rate far higher than comparable changes in Western Europe, the US, and Japan, and matched or exceeded rates achieved a generation earlier by the Northeast Asian "tiger" economies, Taiwan and South Korea. It has been accompanied by urbanization, rising labor productivity, and the emergence of a sizeable middle class, and has to most observers been the region's most visible manifestation of economic growth. It has resulted in Southeast Asia's economies achieving a far more diversified pattern of production and trade than is found other regions of the developing world. Within Southeast Asia, later starters such as Vietnam and Laos now show signs of making the transformation even more rapidly than was experienced by their neighbors.

Figure 4 about here

This rate and pattern of growth has proved remarkably robust despite severe setbacks (notably the Asian Crisis of 1997-99 and the global Great Recession of 2008-10), and periods of great volatility in world markets for important regional commodity exports such as oil and gas, rice, coffee and rubber. In resonance with the structural transformation, the sectoral basis for growth has changed over time. So too has the distribution of gains from growth among factors such as land, labor and capital, and of course among households as owners of those factors. As a consequence, the region continues to provide a fertile ground for theorizing about economic development, just as it has since the end of the colonial era.

Although the foregoing description suggests a group of countries that are homogeneous relative to the rest of the developing world, it goes without saying that each country's development path has been shaped by unique features and conditions. In fact, the divergent features of country experience are as noticeable as their similarities, and understanding these after controlling for inherited factors such as natural resource wealth is an important task for scholars of Southeast Asian development. The Philippines, a promising early leader in development, experienced decades of growth at rates much lower than its neighbors, and in so doing slipped on many measures of economic wellbeing from regional leader toward the middle of the pack. In contrast Vietnam, a much later initiate to modern economic growth, has displayed remarkably rapid convergence on all key measures of wellbeing during its transition from command to semi-market economy. Meanwhile, increasingly close regional economic integration, through institutions such as the Association of Southeast Asian Nations (ASEAN) as well as through adoption of a broadly common regional stance in relation to the Asian and world economies, surely accounts for much of the growth catch-up that can be observed in Vietnam as well as in Laos, Cambodia, and Myanmar, the region's most recent arrivals to market-based development.

The goal of this chapter is to provide an overview of Southeast Asian economics and to introduce some of the key themes to be explored in later chapters. The next two sections offer a brief historical survey of regional economic development since about 1970. The emphasis is on comparisons between 'then' and 'now', especially those phenomena that can be linked to outcomes such as the divergent economic growth rates of the early decades in this era, or the convergence that has occurred more recently. The chapter's focus is more broad, however, than aggregate growth alone. Both the reality and perceptions of the distribution of the costs and the gains from growth are increasingly important political economy issues. And arguably the main point of any survey of development is to identify challenges and opportunities that the future will bring; this is the subject of the fourth section of this chapter. Finally, a concluding section provides an overview of chapters making up the remainder of the volume.

2. Initial conditions

In order to interpret the present, let alone to predict the future, it is necessary first to understand the past. In the generation that followed World War II, as colonialism gave way to modern states and as the geopolitical theater of the Cold War began to take shape, Southeast Asia became the subject of a wealth of studies by economists and other social scientists. Some focused tightly in on local institutions and the behaviors of farm and village communities, which they identified as organizationally distinct from urban (or "modern") populations (Boeke 1953; Geertz 1963).

Others traced the birth and early development of individual nations. Only a few chose to examine the region as an entity. By far the most famous among regional surveys is Gunnar Myrdal's *Asian Drama: An Inquiry into the Poverty of Nations* (Myrdal 1968a), which meticulously documented and compared levels of living and progress in economic growth across South and Southeast Asia. The data and analyses in this landmark work of early scholarship in development economics still provide a baseline for measuring regional progress in economic development.[1]

Possibly the most articulate and insightful appraisal of early economic life in the region, however, comes not from an economist but from a journalist-turned historian: the late Stanley Karnow, in his contribution to the *Life World Library,* a popular American series of coffee-table books. Karnow's volume, *Southeast Asia,* was published in 1962. To revisit it fifty years later is to discover a fascinating mix of continuity and contrast. Karnow documents a region united by geography (he likened the map of Southeast Asia to "a huge jigsaw puzzle") and history, and yet fractured by deep social and economic divisions. Some, such as the dichotomies between countryside and city and between wealthy and impoverished, are as familiar today as they were obvious to observers like Karnow, through the lenses of the *Life* photographers, or in Myrdal's careful tables of data. For confirmation, one need only consider the sharp rural-urban divisions that define opposing factions in Thai politics since 2001, a gulf so wide that it now threatens to bring growth in this otherwise successful regional economy to a halt.

Some other divisions recorded by Karnow are much more surprising to a twenty-first century witness. These are notably the economic and cultural chasms that seemed to divide the region's states from one another,[2] and the contrast between entrepreneurial, development-oriented states and institutions and those seemingly committed to a lethargic, inwardly-oriented status quo.[3]

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[1] Myrdal memorably described governments of the region as "soft" states, meaning that they were characterized by "indiscipline" in legislation, public administration, law enforcement, and the tolerance of corruption. These arise from and reinforce colonial-era weakening of social and political institutions, and give rise to social and economic inequalities which "constitute severe obstacles to development" (Myrdal 1968b: 1129).

[2] In the early 1960s the historian George Kahin likened the region to a Manhattan apartment building: "the tenants occupy adjoining apartments but rarely speak to one another, and their friends are elsewhere."

[3] "Centered in their capitals and remote from the mass of their population, many governments of Southeast Asia are like heads without bodies. In ancient times, these lands had two associated classes, aristocrats and peasants. Today

Lastly, without the depth of perspective that history provides, it is difficult today to comprehend the theme, pervasive in Karnow's writing and that of most of his Western contemporaries, of an unstable, hungry and avaricious "Red" China posing an existential challenge to Southeast Asian states and threatening the wellbeing of their peoples. China remains a daily preoccupation for the region, but it is a very different China and a very different set of issues—far more economic than geopolitical—that now command regional attention.[4]

Economically, the early postcolonial regimes typically rendered economic policies subservient to the seemingly more pressing political tasks of state formation and nation-building. Most of these regimes harbored deep suspicions of capitalism, an economic system that they associated with colonial subjugation. To the leaders of newly independent nations, some of the most appealing alternatives were to be found in the experiences of the Soviet Union and Maoist China, whose quasi-autarkic strategies for the transition from peasant agriculture to industrialization appeared to offer an alternative to the "unequal exchange" of raw materials for manufactures imported from the West. There was also, of course, a more pragmatic motive for mistrust of trade, as Karnow realized in 1962: "As producers of raw materials, Southeast Asians have come to recognize the dangers of dependence on whimsical world markets" (Karnow: 147). During the early post-colonial years, the intensity of Southeast Asia's reliance on trade diminished to historically low levels (Booth 2004).

As the curtain rose on the era of modern economic development, the states of Southeast Asia were (mostly) new, their governments inexperienced, their policies ill-informed and untested, and their basic human needs very great.

3. The long transition

As recently as 1970 (and far later in some countries and areas) the typical Southeast Asian was rural, agrarian, undernourished, unlettered, unbanked, and unconnected to the broader world

the division is between urban and rural folk, and there is scant connection between the two" (Karnow:77). Myrdal (1968a) documents a similar set of impressions in his descriptions of 1960s Thailand, Laos and Cambodia.

[4] Geopolitical issues also persist, however, in ongoing conflicts over ownership and access to large swathes of the South China Sea.

whether through markets, media or migration. Miserable as these conditions were, however, they did not clearly distinguish this region from other developing areas. There were two phenomena, however, that set Southeast Asia apart. First, as home of the fabled Spice Islands and for centuries a key waypoint on global East-West trade routes, Southeast Asia had had a precolonial economy that was far more heavily trade-dependent than can be said for most other countries. Second, according to experts of the day the region's development prospects, along with those of the rest of Asia other than Japan, were globally dim.

One contemporary assessment ranked "Southeast Asia" (meaning the regions we now call South, East, and Southeast Asia) below the Middle East, Sub-Saharan Africa and Latin America on measures of per capita income, population pressure, and economic culture, concluding that "while some of the intermediate rankings are uncertain… in general the degree of poverty and general backwardness is greatest in Southeast Asia and smallest in Latin America" (Enke 1963: 61).[5]

With the region, Malaysia (including Singapore before 1965) was undeniably better off than most. However, even these countries' growth prospects were not uniformly seen as promising, and those of some other regional states such as the Philippines and Burma (now Myanmar) were judged – inaccurately, as it turns out – to be much brighter. One key growth ingredient found to be missing in much of the region was an entrepreneurial spirit. Enke (1963:61) dismissed Asia as having "an uneconomic culture." Finally, the entire region was highly susceptible to economic collapse, whether precipitated by crop failure, government failure, internal conflict, or Cold War-related external aggression. Myrdal, in *Asian Drama,* saw Southeast Asia in the late 1960s as a region in which turmoil was pervasive – except in the mainland kingdoms of Thailand and Cambodia, where as he saw it, "complacent authoritarian regimes administer[ed] a lethargic peasantry."

On international economic integration in about 1970, the region also scored poorly (Booth 2004; Thee 2012). Foreign investment other than in extractive industries was virtually nonexistent. As

[5] I am indebted to Easterly (1995) for identifying this source.

late as 1980, the exports of every country for which adequate data exist were dominated by natural resources and agricultural products. For Indonesia, these contributed 97% of 1980 merchandise exports; for Malaysia 80%, Thailand 72%, and the Philippines 63%.[6]

This pattern of trade reflects comparative advantage of course: the region had for centuries served as a source for exports of natural resource wealth to the larger, more technologically advanced economies of India, China and Japan. But this trade pattern is also a consequence of development policies. In the early post-colonial era most nations of the region pursued development strategies that embodied a substantial anti-trade bias, with tariffs and other barriers that greatly restricted trade in manufactures. As Athukorala (2006) has shown for Vietnam (one of the later-transitioning economies), anti-export bias in trade and domestic policy is a significantly negative predictor of prospects for growth. In Southeast Asia, differential rates of progress in the transition back to global market integration – what Booth (2004) has called "re-linking" – serve to demarcate divergent growth and development experiences.

Among international experts, prognoses of growth were almost uniformly negative in the 1960s, and even much later. Myrdal, in *Asian Drama*, saw the countries of the region (with the possible exceptions of Malaysia and Singapore) as backward, agrarian, and institutionally unprepared for modern economic development, confronting potentially devastating problems of population growth, poverty and food supply. His concerns about Malthusian limits to growth were echoed by numerous influential commentators of the era. These included such influential contributions as Paul Erlich's *The Population Bomb* (1968) and William and Paul Paddock's *Famine 1975!* (1968), which, among other things, dismissed Indonesia as a state that "could not be saved." Yet grow the region did, and through a combination of agricultural modernization, industrial transformation and the relatively sensible application of windfall earnings from oil and other natural resources managed both to increase food supply growth and to maintain the productivity of labor so as to ensure stable or even rising material living standards for their populations.

[6] Source: World Development Indicators Online.

Breaking out of the Malthusian trap was in large part a consequence of the massive technological breakthrough in the production of rice, the regional staple, known as the Green Revolution (ADB 1969; Timmer 1988). New plant types, together with complementary inputs such as fertilizer, irrigation and improved pest management methods made it possible for per capita food supply to grow much faster than land area. Rising yields also increased labor productivity, thereby freeing up a larger part of the workforce for non-farm employment at a historical moment when global demand for labor-intensive manufacturing was poised to boom. And higher and more stable incomes, among other factors, helped spark a rapid decline in fertility, lowering population dependency ratios.

Of course, this historical process exhibited plenty of variation. The Philippines enjoyed far less success in agricultural development and also a much slower decline in fertility. The Mekong countries (Cambodia, Laos, and Vietnam) started down the path of sustained growth a generation later than their regional counterparts, and Myanmar, after half a century of self-imposed isolation and poverty, has only just begun to build the institutional and policy foundations for a modern economy. Overall, however, the region has pulled off a spectacular escape from the Malthusian trap. Twenty-first century students of this part of the world are hard-pressed to reconcile the doomsday predictions of the 1960s with the thriving populations they can see today.

Another more subtle but hardly less negative prediction emerged, ironically, at the peak of the region's growth boom of the late 1980s and early 1990s. With GDP growth rates hitting double-digit levels, Southeast Asia's four largest economies (Indonesia, Thailand, Malaysia and Singapore) were labeled (along with Taiwan, Korea, Japan and Hong Kong) as "high-performing Asian economies" in the landmark World Bank study, *East Asian Miracle* (World Bank 1993). Countries like Thailand and Singapore enjoyed a brief existence as global poster children for economic growth.

In the same years, however, many economists observed that this "miracle" growth was almost entirely due to rather more prosaic processes: the accumulation of new capital and the workforce "gift" of the demographic transition. Krugman (1994) observed that Asian growth of the foregoing two decades could be accounted for almost entirely in terms of increased rates of capital investment, labor force participation, and educational achievement, with little or no additional gain due to productivity growth.[7] As he succinctly put it, the "miracle" depended on "perspiration, not inspiration."[8] As such, he argued, regional growth "has been based largely on one-time changes in behavior that cannot be repeated" (p.71), and diminishing returns to further factor accumulation would ensure that the miracle could not be sustained. As a result, Krugman concluded, "popular enthusiasm about Asia's boom deserves to have some cold water thrown on it... the future prospects for that growth are more limited than almost anyone now imagines."

At the time, this seemed not inaccurate as a look in the rearview mirror of regional development. However, Krugman's prediction of slowing growth rates has not stood the test of time—in spite of mixed results on total factor productivity growth. Rather, the East and Southeast Asian experiences helped to redirect thinking among economists towards new paradigms in which the modalities of international integration—including lower tariffs and transport costs, international factor flows, and above all, rapid movement up the industrial product ladder—help to forestall the onset of diminishing returns to capital investment (Ventura 1997; Schott 2003; Romer 2003). Participation in an expanding and dynamically changing regional economy has sustained growth in these very trade-dependent economies, even in the absence of demonstrable contributions from productivity growth, whether extrinsic or intrinsic (that is, arising endogenously from increasing returns or industry-scale productivity spillovers).

A third pessimistic prediction was based on extrapolation from the 1980s transitions of post-Soviet Eastern European economies. Adjustment from command to market economy involves a so-called J-curve transition in which output, jobs and productivity must all fall (sometimes by a great deal) before the effects of economic restructuring take hold and they begin to rise again. This phenomenon, so clearly observed in the 1990s in Eastern Europe and the states of the former USSR, did not transpire during analogous Asian transitions – those of China and Vietnam in particular. Why this is so remains a subject for more detailed research, but clearly the Asian economies' rapid and decisive reintegration with thriving regional and global markets was a

[7] The latter claim is largely borne out in empirical analyses of regional growth (Collins and Bosworth 1996; Radelet, Sachs and Lee 2001).
[8] NB: This was also the logical outcome of "vent-for-surplus" growth described by the noted Burmese economist Hla Myint (1965).

major contributing factor. In the Chinese and Vietnamese command-to-market transitions, elastic world supplies of intermediate goods, rapidly growing world demands for final goods, and abundant inflows of global investment all helped to cushion economic losses due to obsolescence and facilitated expansion of new, internationally competitive industries.

Fourth, we also know that Southeast Asian resource exporters achieved far greater success in economic growth than is predicted by theories of the so-called curse of natural resource wealth. The curse is said to be of slow economic growth due to a failure to sustain efficient factor use, especially in industrial sectors where the potential for productivity gain is highest. According to Sachs and Warner (2001: 828), "… there is virtually no overlap between the set of countries with large natural resource endowments – and the set of countries that have high levels of GDP ... resource intensity tends to correlate with slow economic growth." Since resource abundance has economic meaning only in relation to a country's trading partners (and indeed, is frequently measured as the ratio of resource-based exports to GDP or total trade), the implication is that for a developing economy, possessing and exploiting comparative advantage in natural resource products can be harmful to growth.

Among resource-rich countries, those in Southeast Asia exhibit the least close fit with the resource curse model. Indonesia, Thailand and Malaysia are almost unique in the developing world for having both high levels of initial resource dependence and also high rates of long-run economic growth (Figure 5). There are many possible explanations, of which the most persuasive is a high rate of success in converting the earnings from natural resource exports into other forms of capital, such as infrastructure, education and the less tangible asset of macroeconomic stability, that create fertile conditions for a transition to industry and thus, reduced dependence on resources as an income source (Coxhead 2007). This is not to say that the region's economies, and especially Indonesia, have not experienced Dutch Disease, the attenuation of growth in non-resource tradable sectors that often follows a commodity export boom (Warr 1985)—nor that they will not experience it again the future. They have simply been more adept at recognizing the symptoms and addressing them in a timely way through policy. And they have avoided (for the most part) a major corollary of the resource curse: military conflict over oil, diamonds and other mineral deposits and the revenue flows they engender. In sub-Saharan Africa, by contrast, twenty-eight of 50 countries have been involved in war or civil war (or in some cases, both) since 1980, generating over 9m refugees or internally displaced persons and accounting for 88% of conflict fatalities worldwide since 1990.[9] The costs of war, in terms of foregone growth, are massive.

Figure 5 about here

A fifth pessimistic prediction about Southeast Asian growth, and one upon which remains moot, comes from contemporary analysts such as the Malaysian economist Jomo K.S. (2003). This view regards regional growth booms as driven largely by external factors, especially trade and FDI, and as lacking the internal dynamics and governance capacity required to sustain them in the longer run. Jomo's discussion of regional development through the early 2000s concluded that

> "…the Southeast Asian component of the East Asian Miracle…was inferior to the rest of the region's economic achievements in terms of growth, inequality, industrialisation, policy formulation and implementation, human resource development, as well as development of industrial and technological capabilities. […] Unless adequately addressed, these failings will limit the likelihood of rapid future growth and structural transformation associated with the East Asian Miracle" (Jomo 2003:17).

The core of this argument is pessimism about institutional capacity for good economic governance, a broad term used to capture the essential qualities of economic and political institutions required to support long-run growth.[10] This idea reflects an important branch of thinking among development economists in which institutions, rather than geography, culture or "luck," are primarily responsible for differences in comparative growth (Acemoglu, Johnson and Robinson 2005). Though measures of institutional quality by their nature very imprecise, no Southeast Asian country other than Singapore displays any special institutional strengths in international comparisons. Corruption, for example, is thought to have a strongly negative effect on potential for economic growth, yet all Southeast Asian countries except Singapore rank low in

[9] http://www.globalissues.org/article/84/conflicts-in-africa-introduction, accessed 8 June 2014.
[10] Institutional pessimism is an enduring theme. In 1978 the Asian Development Bank's review of prospects for regional success in agricultural development bemoaned the "growth-retarding effects of production technologies and the institutions serving agriculture when these are not properly aligned with each other" (pp. 319-20). This report called for strong and pervasive state actions, yet condemned states as elite-dominated, incompetent and possibly corrupt, and capable only of "responses to short-term situations… insufficient consideration was given to assessing the implications for long-run orientation of policy" (p.9).

international comparisons of corruption perceptions (Table 1). As Table 1 also shows, other than Singapore the region generally receives poor scores and rankings on institutions for economic governance. Yet as we have seen, Southeast Asia has succeeded in achieving and maintaining a truly impressive rate of economic growth. If corruption is so high and measures of the quality of economic institutions so low, how is it that large, low-income countries like Indonesia and Vietnam have outperformed the rest of the developing world on growth?

The institutions argument certainly raises puzzles about the rate and persistence of past growth in the region. Perhaps the commonly used measures of institutional strength don't capture essential qualities relevant to growth and stability. Or perhaps there are interactions among institutions, culture and geography in which weaknesses in the former are compensated by advantages in the latter. These interactions would not necessarily appear in the kinds of global-scale cross-country analyses favored by those seeking generalized or global explanations for economic growth and development.

Finally, we know that economic and political institutions evolve over time and under changing conditions, so what predictions for the future, if any, can be made with confidence? One possibility is that rapid growth creates its own compensating circumstances, for example by reducing pressure on the distribution of resources, which in turn affects de jure and de facto political power, the drivers of change in economic and political institutions (Acemoglu et al., 2005). If so then the region is poised to enter a crucial period in the early twenty-first century, in which lower GDP growth rates generate greater tension between competing policy and political economy goals. We outline some of these possibilities in the next section.

In its transition from poverty to middle income over a half-century, Southeast Asia has managed to avoid many of the economic growth traps that have impeded progress in other parts of the developing world. There is, however, tremendous variation around this overall trend, and moreover, successes in the past do not guarantee continued progress through middle income in the future. These two concerns are central to much of the content of this handbook.

4. Southeast Asian economies today

Contemporary Southeast Asian economics is an encouraging mix of growth, economic stability, and improving standards of living. The Philippines, for many years the laggard among the large regional economies, has registered solid growth since the mid-2000s. Even Myanmar, one of the world's poorest economies after 50 years of self-imposed isolation, has begun making rapid strides toward reintegration and growth. The region's long transition continues.

In the evolution of today's Southeast Asian economies, the regional economic crisis of 1997-99 was a turning point. The "miracle" years had seen all the region's large economies except the Philippines growing at well above their trend rates (Figure 6a). Increasing confidence in the continuity of growth had encouraged governments to relax rules on capital inflows. As a result, ever-larger injections of short-term capital into domestic financial systems helped fuel speculative booms in stock markets, property and construction. These inflows of portfolio capital and foreign loans were largely unhedged because they were "insured" by buoyant growth and by public commitments to fixed (or at least predictable) exchange rates. The latter were promises that were relatively easy to keep during a period of rapid growth with stable domestic prices. By the mid-1990s, however, export-oriented manufacturing booms began to drive up labor costs and create costly infrastructural bottlenecks, causing expectations of profit margins to decline. This trend, plus current account deficits due to the capital inflows, undermined confidence in exchange rate stability, and starting in early 1997, liquid capital began to exit the region. With foreign reserves nearing exhaustion, exchange rate anchors began to drag, and the collapse of regional asset price bubbles was accompanied by a brief but intense liquidity crisis in which many thousands of jobs and livelihoods were lost. As Figure 6a reveals, the crisis was a sudden stop for all economies, although in the Philippine case low rates of prior capital inflow and growth meant a correspondingly shallow recession.[11]

Figure 6 about here

[11] To paraphrase one Filipino commentator, "we only had a little boom, so we only had a little bust."

The recession was unprecedented in nature and depth for much of the region (Indonesia and Thailand had not experienced even one year of recession in three prior decades). It exposed internal vulnerabilities that had been disguised by years of rapid growth. These included policy failures as well as inherent weaknesses in economic institutions, especially where the will and capacity to respond to a sudden external shock were concerned.[12] The crisis also precipitated political upheavals, most catastrophically in Indonesia, where *krismon* ("monetary crisis") quickly spilled over to *kristal* ("total crisis"), a period of chaos and violence culminating in the collapse of the 32-year New Order regime and the beginnings of a transition to democratic governance.

The crisis also led governments of the region to re-think economic policies, especially although not exclusively in the areas of exchange rate and monetary policy and governance of financial systems (Corden 2007). It stimulated moves toward greater regional economic and financial integration, and to the extent that it was fuelled by loss of competitiveness in labor-intensive manufacturing, the crisis also brought into sharp relief the challenge posed by a rising Chinese economy (Eichengreen and Tong 2005; Coxhead 2007).

The later-developing Mekong economies were never as open to international capital flows as their larger and more advanced neighbors. This afforded them a degree of insulation from the capital market shocks that precipitated regional recessions (Figure 6b). Their GDP growth rates fell briefly below trend, but as quickly recovered again. Overall, these economies have experience far smaller variation in GDP growth (and higher overall growth rates) since beginning their economic reforms.

The decade following the crisis, from about 2000 until the onset in 2009 of the global Great Recession, saw a gradual but steady recovery throughout the region. However, the largest ASEAN economies have never returned to the heady GDP growth rates of the Asian Miracle years (Figure 6a). Lower growth rates have had fiscal and political implications. With leaner

[12] There have been many excellent economic accounts of the crisis and its immediate aftermath. See, for example, Corden 1999, McLeod and Garnaut 1998, and for Thailand, Warr 2005.

economic times, budgetary "fat" such as subsidies on fuel prices have become unsustainable, and attempts to lower subsidy rates have been the cause of political unrest. And in Thailand, the combination of constitutional changes leading to populist politics based on generous subsidies to rural constituencies, together with reduced tax revenues from lower rates of economic growth, has exposed deep societal divisions over the distribution of income and opportunity. This has brought with it increasing levels of extraparliamentary protest, conflict, violence, and political instability.

More positively, ASEAN economies now see more clearly the benefits of internal and external coordination in trade, capital markets and external economic relations. ASEAN, the primary vehicle for regional cooperation, has taken on a far more prominent and pro-active role in Southeast Asian economic life.

In the second decade of the 21st century, nearly nine out of ten Southeast Asians live in countries classed as "middle-income." Compared with their grandparents they are immeasurably healthier, wealthier, better-educated and more secure. Despite this great progress, however, many still live just one missed paycheck or one major medical bill above the poverty line—and in societies whose social safety nets cannot guarantee to catch them if they fall. Looking to the future, most can see continuing improvements in their levels of living. But how fast this improvement will be, and over what period of time it will extend, is much less certain.

5. Overview of this volume

Why have a book on Southeast Asian economics? The very term "Southeast Asia" is a recent creation, a convenient catchall for an Allied theater of war in WWII (Karnow: 11). However, the last four decades have seen a strongly increasing trend in regional economic integration and policy coordination, and provide increasing evidence of positive spillovers in growth, public administration, political systems and more.

Is there a specifically *Southeast Asian* economics? Strictly speaking, the answer must be "no." However, there is a case that the regional experience embodies an important and interesting specific *configuration* of factors: resources, geography, and history, trade and international investment, and the proximity of large, dynamic neighbors. This configuration naturally brings certain themes to the fore, and in this respect Southeast Asia does seem sharply different, if not unique among developing regions. Most prominent among these themes are those relating to the region's unusually long and deep levels of global and market integration and unusually high proximity to large, dynamically growing economies. Global market integration, beginning long before the great European voyages of discovery, exposed Southeast Asia from very early on to interactions with economies that differed dramatically from it in terms of endowments, technology and tastes. This meant that prices for commodities and services produced and consumed in the region have changed greatly with changes in its exposure to trade with other world regions.[13] Proximity to the world's largest (at times) and (at times) most dynamic economies further reinforced the importance of trade, which fluctuates with greater volatility than underlying economic conditions. Hence, at some points in history the region's giant neighbors have catapulted the Southeast Asian economies onto "miracle" growth paths, and at others plunged them deep into recession.

These themes pervade the story of Southeast Asian economic development. Williamson (Chapter 2) surveys half a millennium of regional interaction with the world, primarily through trade, and explores the ways in which precolonial and colonial-era trade affected incomes and development. Booth (Chapter 3) picks up the thread in the colonial era, which affected every country except Thailand, and follows it through postwar decolonization and the establishment of modern nation-states. Her chapter stresses both the late colonial-era mechanisms of economic growth, and the difficult transition to post-colonial policies when trade and foreign investment, the long-run keys to regional growth, came to be regarded by newly minted regimes with deep suspicion, ushering in a brief era of "delinking" from the world economy.

In Chapter 4, Phung, Coxhead and Lian present a quantitative exploration of the sources of modern Southeast Asia's contemporary economic growth. As is standard in this type of research, their analysis identifies contributions from growth of endowments of capital, labor and skills.

[13] Compare Hansen (2012)'s revisionist history of the overland Silk Road, in which the author argues that paper, not silk may have been the most important commodity traded—and emphasises the concomitant spread of metals and metallurgy, technologies and ideas. Southeast Asia sits astride the maritime silk route and experienced the same rich mix of commodity trade items (Reid 1993).

However, they also identify important spillovers from growth booms in the region's large and dynamic neighbors in Northeast Asia. These Northeast Asian booms conferred positive growth externalities on the region, in addition to serving as powerful stimuli to investment and growth-enhancing structural changes in employment and output. Proximity to Northeast Asia, in both a geographic and an economic sense, was a geographical advantage not shared by other regions of the developing world.

The next nine chapters in this volume address factor endowments and economic organization and their contributions to economic growth. Appropriately for a region that was almost entirely agraraian just two generations ago, we begin with a survey of agricultural development (Timmer, Chapter 5). Also appropriately, for a region whose largest country was dismissed two generations ago as structurally unable to feed its own population, this survey views agricultural development primarily through the lens of food security. Timmer documents the region's convincing escape from imminent Malthusian disaster, mainly though not wholly by means of the Green Revolution technologies that so greatly increased the productivity of rice cultivation. Looking at the present and the future, Timmer notes large ongoing changes in demand (through income-driven dietary transformations) and markets, especially the rise of corporate distribution channels such as supermarkets. While food supply is no longer the pressing issue that it once was, the future holds significant challenges from climate change and from competition for land from industrial crops, such as oil palm.

Shively and Smith (Chapter 6) address the natural resource and environmental basis for growth. In spite of rapid industrialization, Southeast Asia's poor remain heavily reliant on land and other natural resources. It is logical for poor countries to exploit their comparative advantage in natural resources in order to get started on growth, but the momentum of resource depletion and damages to environmental quality may be virtually unstoppable, especially when foreign demand is strong and domestic regulatory institutions are weak. Their chapter concludes by emphasizing the synergistic interaction of economic growth with institutional innovations to regulate resource depletion and environmental damages. Success in economic growth relieves some of the pressures to exploit the resource base, and this in turn can support the move to a more sustainable growth trajectory.

Rapid and pervasive industrial growth is one of the most visible and unusual features of Southeast Asian development. The origins of industrialization in the region are well known, but in Chapter 7, Athukorala and Kohpaiboon pick up a more contemporary account of the transition from "traditional" manufactures of final goods to participation in regional and global networks of vertically fragmented producers. Trade in parts and components, mainly of electronic, electrical and machinery products, is the fastest-growing category of trade in East Asia, and brings with it new forms of industrial organization and sources of dynamic economic growth. However, not all countries in the region are equally well prepared to take advantage of the new patterns of production and trade, and this raises interesting questions about future divergence along the industrial growth path. A similar story emerges on the counterpart flow, of investment capital (primarily, though not entirely, into the region). Sjoholm (Chapter 8) appraises the sources and impacts of FDI flows. Among his findings is an important political economy observation, that of synergies between policies and institutions relevant to FDI and economic growth. Once again, country-level differences in attitudes toward FDI—some of them the enduring legacies of the fight against colonialism—introduce much heterogeneity within the region.

Wignaraja (Chapter 9) takes the account of industrialization down to firm level, with an empirical study of firms' use of regional trade agreements (RTAs) in their business dealings. RTAs have been among the key vehicles for reducing trade barriers both within Southeast Asia and to the region's major trade partners. The study of firms in three large countries, Indonesia, Philippines and Malaysia, asks quantitatively how valuable these RTAs are as stimuli to commercial activity. He finds surprisingly low take-up rates of RTA concessions, with a variety of reasons emerging across the surveyed firms and countries.

Attention in the book then turns to the region's most important asset, its labor. Jones (Chapter 10) provides a masterful and very thorough survey of population and demographic trends. His study highlights the momentum imparted by years of rapid population growth, even as fertility rates in the region have declined, in almost every case, to less than replacement rate. Horioka and Terada-Hagiwara (Chapter 11) explore how demographic trends (mainly) have determined variation in domestic savings rates. As populations age (led by Singapore and Thailand, the countries with the lowest birth rates), savings rates can also be expected to decline, and this will in turn have macroeconomic implications as current account surpluses diminish and dependence on imported capital (FDI) increases.

In Chapter 12, Phan and Coxhead document progress in increasing educational attainment. It is widely believed that Southeast Asian economies owe much of their success to human capital investments. This chapter finds, however, that the region is not exceptional in that regard—and indeed, by comparison with Northeast Asian economies such as Taiwan and Korea at comparable stages of their own development, most of Southeast Asia lags behind. Education and human capital are perhaps the strongest predictors of escape from the middle income trap, so these findings are not encouraging for the region as a whole. Finally, Sugiyarto (Chapter 13) turns attention to the all-important topic of labor mobility. Capital investments that sustain industrial and urban growth are of course highly location-specific; therefore, if a country is to take advantage of the opportunities created by capital, its labor force must move. Urbanization is the most common expression of labor mobility, but the region has also become a significant exporter of labor to other world regions, and the remittance flows from both types of labor movement have helped distribute the gains from spatially unequal growth more broadly throughout national populations.

Sustained poverty alleviation is arguably the most significant indicator of progress in economic development, and in this respect Southeast Asia's achievements have been dramatic. In Chapter 14, Warr documents poverty trends in the region. He notes in particular the strong relation between overall growth and poverty reduction. More surprisingly, he finds that in this region the principal sectoral driver of poverty reduction has been agricultural growth, not industrial development. This, he concludes, is due to the extreme labor-intensity of agriculture relative to industry, even in its more labor-intensive forms. These findings are a reminder that despite much progress in economic growth labor, mostly in its raw (unskilled) form, remains the primary income source for virtually all of Southeast Asia's poor.

The quality and timeliness of policy innovations and reforms as drivers of economic growth are often underappreciated in the developing world. Hill (Chapter 15) effectively dispels that notion for this region. With the support of several well-chosen case studies, he documents the interactions of policies (both good and bad), the institutions that underpin them, and the outcomes they engender. His chapter concludes with a number of general conclusions on the political economy of economic development in this part of the world.

The final four chapters of this volume address issues of increasing importance in the region for the foreseeable future. Nobles (Chapter 16) picks up the demographic thread once more. She notices that alongside the demographic transition through which most of the region is rapidly passing, there is an accompanying transition in disease and health demands. She notes in particular the dyssynchrony of development at a subnational level: within countries, some regions are aging fast while others continue to experience high fertility and population growth, creating a dual burden of demands for both old and young populations. At the same time, the very rapid growth of regional incomes means that countries that still suffer from "third world" diseases like tuberculosis and under-nutrition are simultaneously experiencing rapidly rising rates of "first world" ailments like diabetes and cancer. This places even more stresses on the design, funding and delivery of health services, creating a second, fiscal type of health-related "dual burden."

Returning to the regional economy, Hill and Menon (Chapter 17) explore the recent and emerging pressures for greater regional integration. In a world of network trade and covariate macroeconomic shocks there is a large premium on lowering barriers to cross-border trade, investment and financial services. Yet these are among the most difficult deals to make. Hill and Menon zero in on the role of ASEAN, an entity that has matured from a primarily political mandate toward a much broader and far-reaching set of goals for economic integration, including the formation of a regional financial safety-net.

In Chapter 18, Nidhiprabha documents the impacts and policy responses to the Great Recession, also known as the global financial crisis (GFC). Coming just a decade after the onset of the Asian crisis (1997-99), the GFC tested the robustness of macroeconomic policies adopted in response to the earlier crisis. In general, the GFC had a much lesser impact on Southeast Asian economies, although whether this was due to their policy innovations, or the stabilizing influence of continued expansion in the Chinese economy, or because the GFC (unlike the Asian Crisis) was an external shock, is as yet unclear. What is sure is that the nature of the region's macroeconomic environment is constantly changing, most recently with the rise of China not only in trade, but also as an influence over financial markets and exchange rates

Finally, Coxhead, Thee and Arief draw together some thematic threads of the volume and discuss some key areas in which Southeast Asia will continue to face growing economic and policy challenges in the future. These include continued labor force and human capital development, finding new and efficient ways to cope with global economic volatility, managing the tensions between economic growth and inequality, and formulating responses to global climate change and especially its regional expressions in rising sea levels and greater intensity of severe weather. Although the region has achieved great progress in economic growth and development, the path ahead to sustained, and sustainable improvements in human welfare is by no means clear. There is much that remains to be learned.

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Table 1: Corruption perceptions and economic freedoms in Southeast Asian countries

	Corruption[a] (0-100 scale)		Indices of economic freedoms[b] (1-10 scale)					
Country	Score 0-100	Rank (N=177)	Legal system & property rights	Rank (N=144)	Freedom to trade internationally	Rank (N=144)	Government Regulation	Rank (N=144)
Cambodia	20	160	4.6	95	7.3	65	6.5	101
Indonesia	32	114	4.5	105	6.8	93	6.3	112
Lao PDR	26	140						
Malaysia	50	53	6.9	34	7.3	66	8.0	20
Myanmar	21	157	3.2	134	1.8	144	4.4	143
Philippines	36	94	4.4	110	6.7	96	6.9	74
Singapore	86	5	8.4	6	9.4	1	8.9	4
Thailand	35	102	5.4	79	6.8	88	7.0	65
E. Timor	30	119						
Vietnam	31	116	5.9	59	6.3	109	6.5	105

Sources: (a) Transparency International 2013. (b) Gwartner, Lawson and Hall 2012.

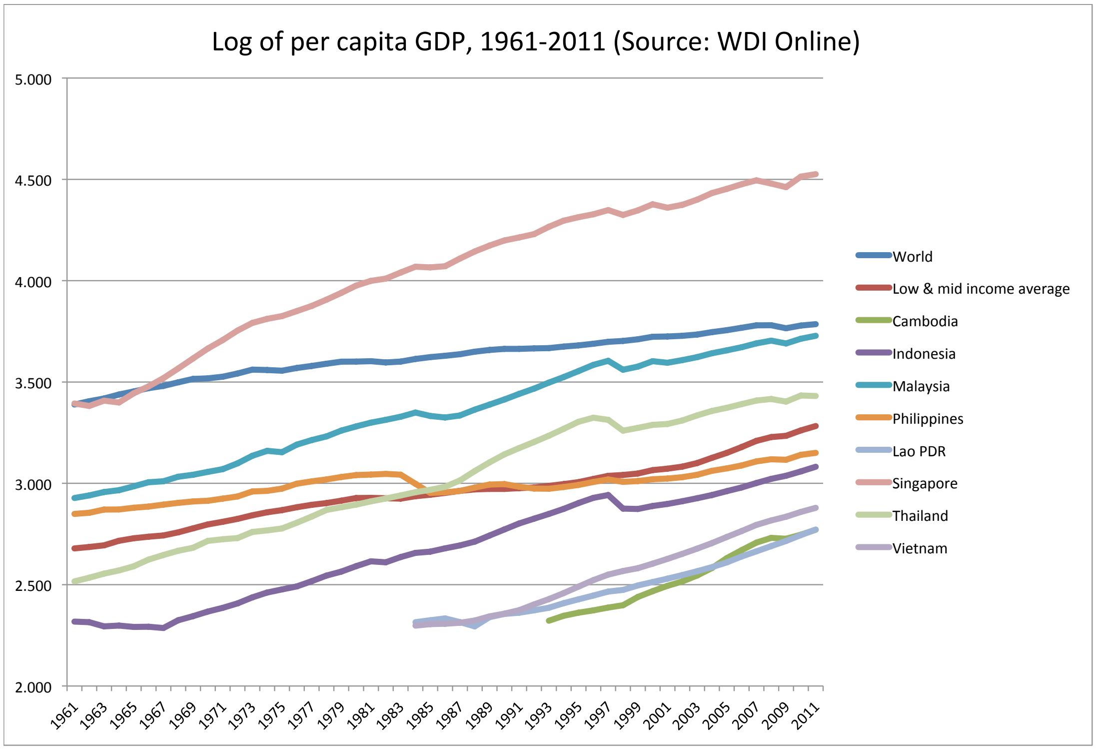

Figure 1: Growth of per capita income

Source: World Bank: World Development Indicators Online

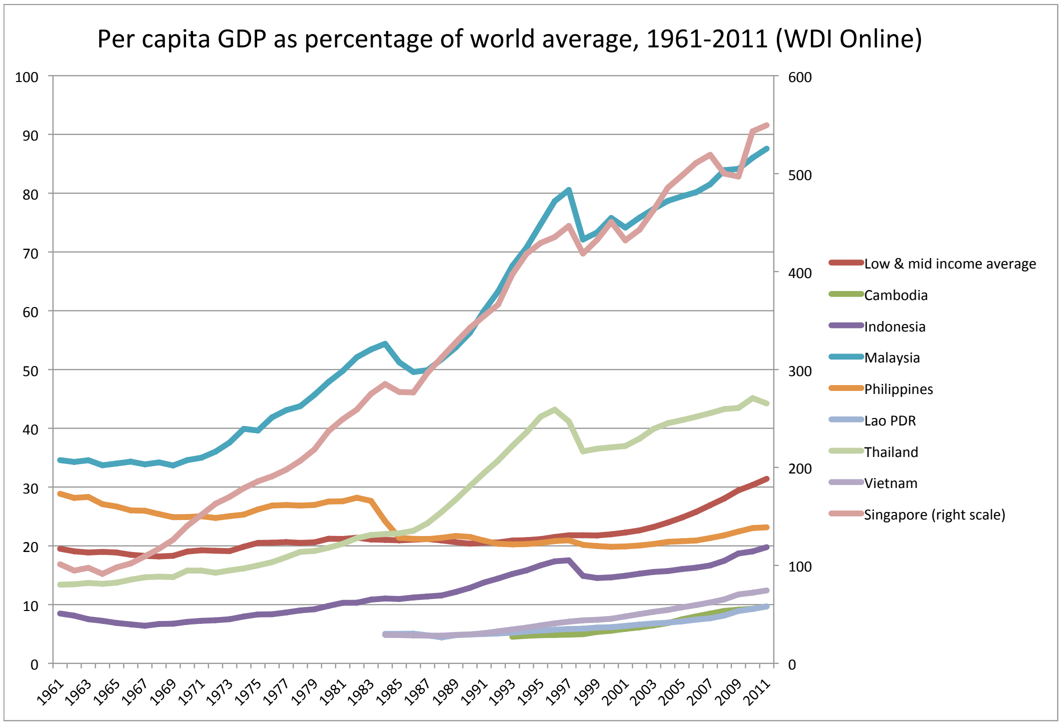

Figure 2: Per capita income as percentage of world average.

Source: World Bank: World Development Indicators Online.

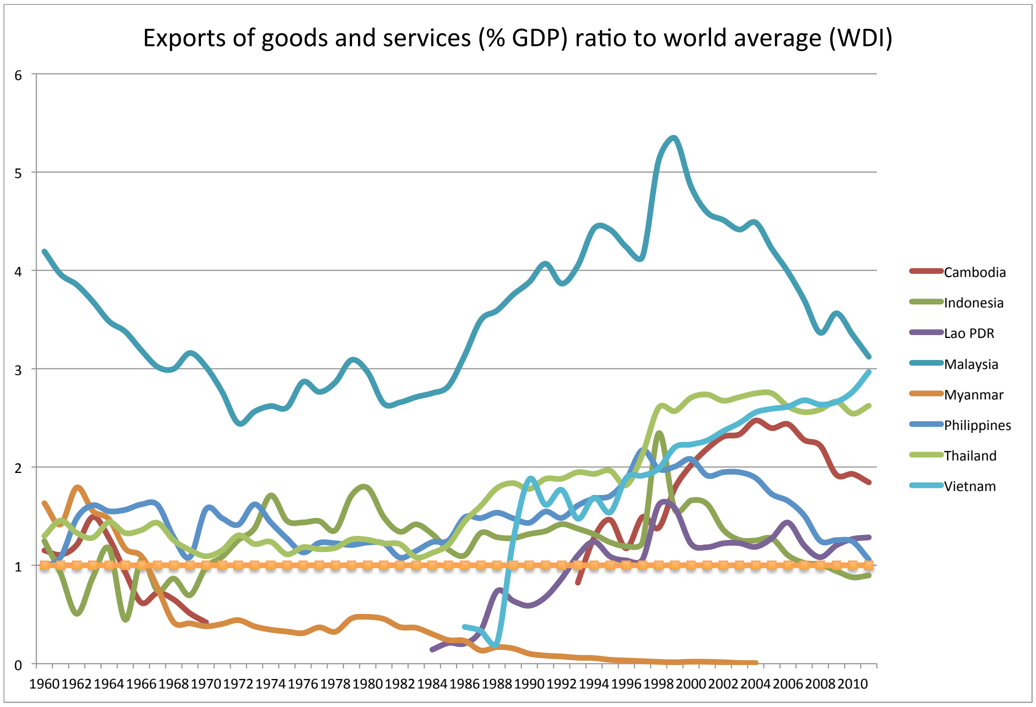

Figure 3: Export intensity relative to world average

Source: World Bank: World Development Indicators Online.

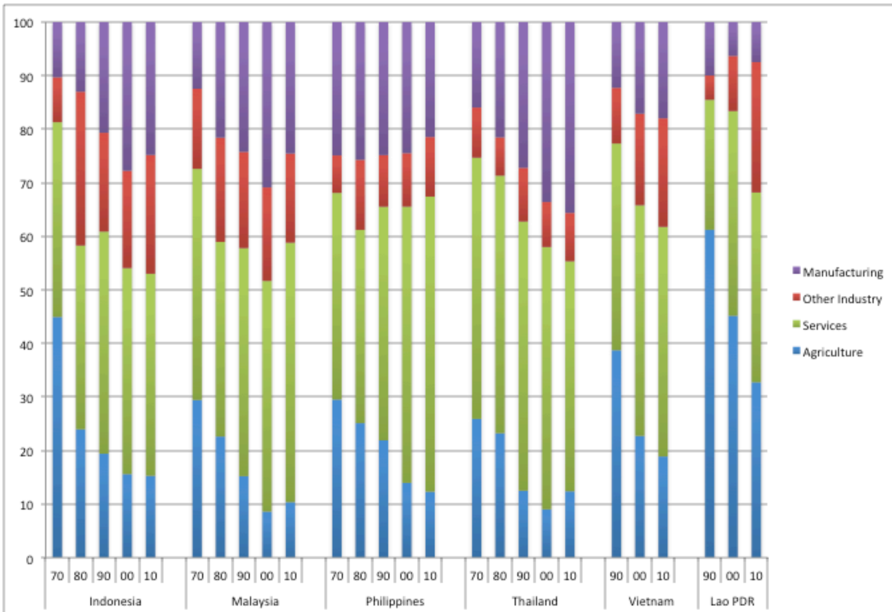

Figure 4: Trends in sectoral structure of value added, 1970-2010

Source: World Bank: World Development Indicators Online

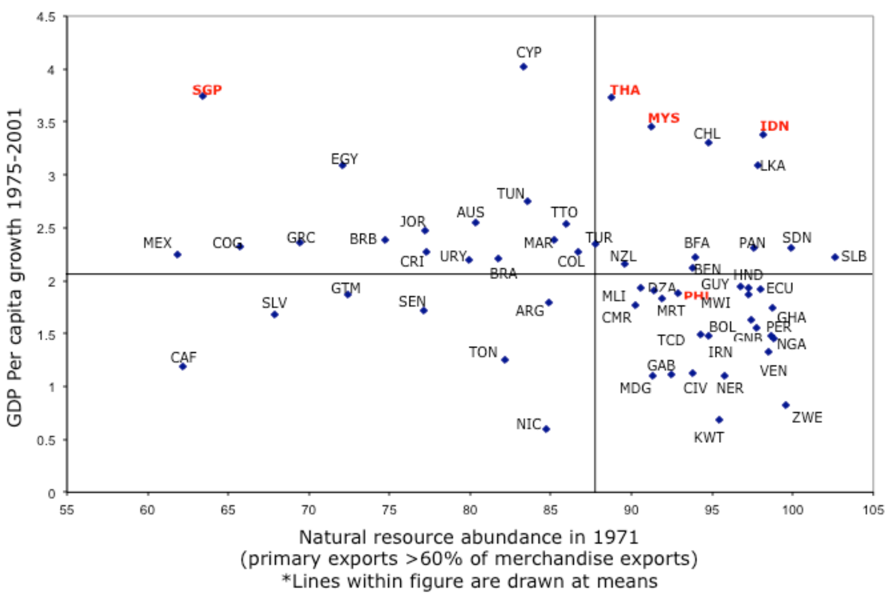

Figure 5: Long-run growth among resource-abundant economies (source: Coxhead 2007)

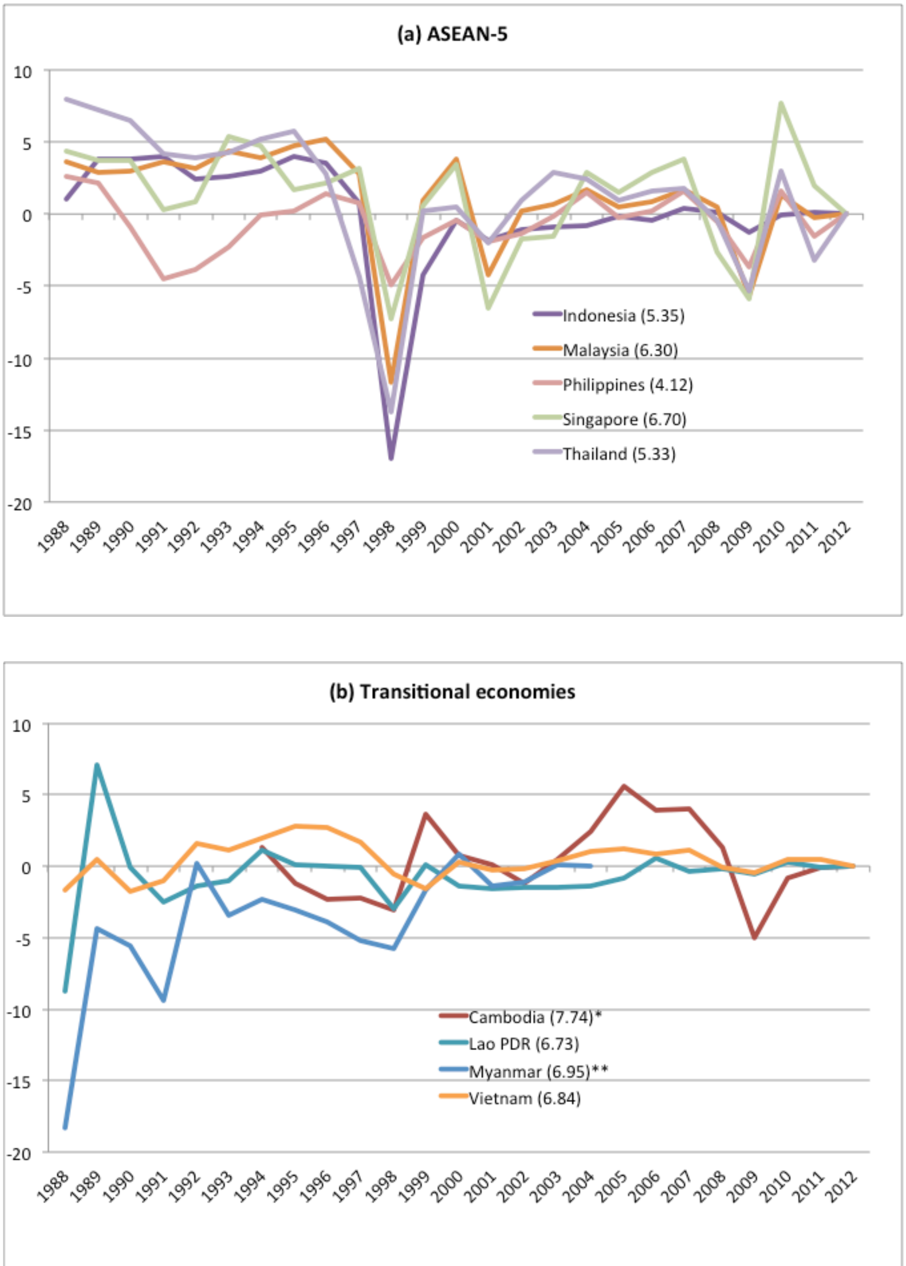

Figure 6: GDP growth rate deviations from long-run average (% per year), 1988-2012 (Average growth rates shown next to country names)

Source: World Bank: WDI Online

Note: *Cambodia data 1994-2012; **Myanmar data 1988-2004.