

EASTERN ECONOMIST PAMPHLETS

General Editor : E. P. W. da COSTA

29

**THE ECONOMIC DEVELOPMENT OF
SOUTH-EAST ASIA**

by

E. P. W. da COSTA

and

K. RANGACHARI

Re. 1

EASTERN ECONOMIST PAMPHLETS

General Editor : E. P. W. da COSTA

29

**THE ECONOMIC DEVELOPMENT OF
SOUTH-EAST ASIA**

by

E. P. W. da COSTA

and

K. RANGACHARI

GENERAL EDITOR'S PREFACE

At the request of many readers of 'The Eastern Economist' certain articles which appeared in the Annual Number 1954 on the Economic Development of South-East Asia have been drawn together and made available in a more convenient form and at a much more convenient price.

These articles were written by the present Editor of 'The Eastern Economist' and Mr. K. Rangachari, Senior Assistant Editor. They now appear over their joint names.

1st March, 1955.

CONTENTS

	Page
1. Introduction	... I
2. The Problem of Production	... 4
3. The Problem of Capital	... 7
4. The Problem of Payments	... 10
5. Inter-Regional Trade Agreements	... 13
6. Industrial Enterprise—Private and Public	... 16
7. Development Patterns : Community Approach	... 20
8. Old Faiths And New Perspectives	... 22

I. INTRODUCTION

THE purpose of this paper is to set out some thoughts on the economic development of South-East Asia at the present time. The difference between this approach and the approach of planning in the various countries of this area might be described by saying that the approach here suggested is regional while most countries of this area are planning on a strictly national basis.

And yet there is in some sense a South-East Asian Plan. But this—the Colombo Plan—fails properly to qualify. The first criticism of the Colombo Plan is that it is an envelope of national plans without any thought of the problems of inter-regional development, that is, development by co-operation between the countries themselves. This is not to suggest it was entirely mistaken on that account. The Third Annual Report of the Consultative Committee on Economic Development in South-East Asia, which has just been issued, will indicate that, notwithstanding its limitations, the Colombo Plan has given precise form and shape to the economic development in this area. To say this is not, again, to admit that the form and shape should be continued: both need changes.

The first need is a change in philosophy; the second a change in size. It is argued in the pages that follow that a true plan for South-East Asia must be conceived differently and on a much grander design.

The Philosophy of the Colombo Plan

Broadly speaking, the philosophy of the Colombo Plan was based on the application of a catalyst to change the form of static economies into economies which, slowly and

ponderously, would provide the means of their own development. This was because when the Colombo Plan was first conceived, all the economies of South-East Asia were believed to be static with an obstinate attachment to stationariness both in agricultural and industrial production. It was believed that capital and technical skill were both necessary to break this stationary state and, in so far as there was some competition between the two, the weightage was more on the side of capital than on technical skill. It is now clear in the light of the experience of some countries, particularly India, that the impulse to break the stationary state might come about by quite different means, and in particular with much less expenditure, particularly of the foreign kind.

The Indian Example

Both Indian industry and Indian agriculture, for example, have exhibited in the last two years dynamism of a kind which makes the assumptions of the Colombo Plan unwarranted and the size of the Colombo Plan deeply inadequate. The official Interim Index of Indian Industrial Production has risen steadily from 105 in 1950 to a figure of 152 in September 1954. In a matter of the last four years, Indian industrial production has risen by about 50 per cent. This has been accomplished largely by the effort of industries in which there was no new foreign capital and no new technical skill. At the same time, agricultural production has risen in India by about 20 per cent under conditions where foreign skill was of a very small order and was measured by such small capital-consuming techniques as the Japanese method of rice cultivation.

By Their Own Bootstraps ?

The Indian example seems to suggest that in India certainly, and probably in most countries of South-East Asia, the capacity for under-developed countries to raise themselves by their own bootstraps is very large. In a sense this experience runs contrary to a classical theory of economics

for under-developed countries. The familiar vicious circle that poverty and low production must go together is now shown not to be a necessary condition. India's rate of capital formation has risen significantly in the last two years notwithstanding the fact that a great majority of her people are still desperately poor. Secondly, it is now seen that no arduous virtuous circle is necessary before productive investment takes place. The familiar chain reaction of classical economists which flowed from 'good climates' for saving and investment is not necessary, although it is a desirable condition for economic advance. Against the chain of saving or capital formation, investment with a good opportunity of profits, and then a rise in real incomes, there is now available the possibility of direct public investment which raises incomes straightaway. The Indian experience can be applied elsewhere. There are indications that in vital points, notably in the purchase of South-East Asia's strategic materials, rubber and tin in particular, assistance by the Free World will be necessary. But, by and large, it is possible for a great plan of economic development to be set to work without major foreign capital assistance.

2. THE PROBLEM OF PRODUCTION

ONE attractive approach to the problem of production is to examine whether or not an increase of production can be obtained by planning peak production for each commodity in each country as a first stage in development.

In the case of rubber, for example, the peak figure of production was in fact attained in 1953 in only three countries. In other cases, both the years 1952 and 1953 have recorded significant decreases from the peak figure. If the peak of natural rubber throughout the area be taken at the monthly average of 157,000 metric tons, present production might not represent a figure of more than 139,000 or a decrease of 13 per cent. Similarly, in the case of tin concentrates, peak production in this area has been as high as 9,645 tons in monthly average terms, but at the present time average production is about 8,600 tons only, a decrease of 10.7 per cent. Even in the case of tea, where there has been a great windfall as a result of record prices, present production runs about 8 per cent below the peak figure for South-East Asia.

Natural rubber and tin concentrates are here merely illustrations in the total picture. In practically every field, not excluding the central field of rice production, South-East Asia is now running considerably below its peak figure. On the basis of average figures, it might be said that in total production, both in agriculture and industry, South-East Asia is running somewhere about 10 per cent less than a figure based on its best past performances. Here at least it cannot be said that a 10 per cent rise in the specific directions in which there has been a fall is an impossibility. This does not imply that a rise will take place automatically. But it certainly can be planned as a first stage in a plan for

production in this area. There should be examined, in every single case, the reasons for a fall in production and there should be a determination by collective action in the area to restore peak production in every field.

In a broad sense, it may be said that the major limitation in these cases has been the fall of demand. Therefore a plan for South-East Asia, in order to restore production at current prices, must be designed to produce demand at current prices or at prices reasonably close to them. Alternatively, by the application of new techniques or additional investment, costs must be brought down to raise demand in the process. Conditions will naturally vary from industry to industry; but it should be clear here that the difficulties cannot be intrinsically very great. The example of India seems to suggest that with greater determination they can be readily overcome; world demand, after a lag, is rising again.

In the case of items which are largely for export, such as rubber and tin of Malaya and Indonesia or the tea and jute of India and Pakistan, the international picture is far more important than the inter-regional one. Here some form of trade agreement between South-East Asia and countries outside the region will be essential. On the other hand, since South-East Asia is herself a consumer of most of her own rice and food grains, there is much more scope in some cases for a purely regional arrangement.

Second Stage

This takes us only to the end of the first stage. The problem of production cannot be allowed to rest only on the attainment of past peak levels. The second stage of a plan in South-East Asia must involve a bold re-calculation of capacities which can be built in before 1960, that is, in the next five years or so. In the case of India, the dimensions of the Second Five-Year Plan will involve an expenditure not less than 50 per cent above that of the first Five-Year Plan.

In real terms, this is likely to involve a doubling of industrial production, a rise of something like 30 per cent in agricultural production and a doubling of capacity in transport. There is a presumption that similar targets can be established for most countries in South-East Asia.

In respect of most commodities of importance, world demand may be presumed to rise adequately. In the case of some vital materials of South-East Asia, notably rubber and tin, this is certainly the case. The Paley report in the United States, for example, sets out the belief that natural rubber would need to rise by 50 per cent to satisfy the United States import demand by 1975 and tin would similarly rise by a sixth. This is only an estimate of United States demand and it is inconceivable that demand elsewhere would remain stationary. In the case of India, the doubling of industrial production is almost certainly likely to express itself in a doubling of both rubber and tin imports. Wherever possible, it should be possible by a series of international or inter-regional agreements to make sure that demand at a figure considerably higher than at present is guaranteed.

3. THE PROBLEM OF CAPITAL

ALTHOUGH capital in underdeveloped countries does not now appear to be the vicious obstacle it was three years ago, it would be foolish to make light of capital difficulties. Broadly, it may be said that there are three lines from which capital can be found. The first of these is domestic saving, the second, private foreign capital and the third, foreign aid. In respect of domestic capital formation, there is now to be considered the dynamic effect of public investment rising at a significant rate. There is something in the evidence of the Indian economy in the last two years to suggest that the rate of capital formation in India has been significantly assisted by government payments. This is no more than a repetition of Indian experience in World War II where it was shown that where payments were prompt a virtuous circle might be established by which public expenditure stimulated deposits and thereby advances, and also aided public and private savings, out of the increased income which it generated. Of all the three lines of stimulation of capital formation in all these countries, this must be reckoned the most important.

Deficit Financing

It is also believed that the weapon of deficit financing has an assured place in the public financing of the development of plans in all countries in this area. It would appear that contrary to usual belief, where deficit financing is employed on productive schemes, the inflationary factor can be reduced almost to nothing. This is largely because in most countries in this area the elasticity of savings is high. In

the first Five-Year Plan in India, it was assumed that about half the increment of output would be saved. Recent studies of India's rate of capital formation in the last two years have indicated that this assumption in Indian conditions was well justified. It is likely that the rate of savings out of increments in output in other countries of South-East Asia would be rather lower than in India. It may be that on an average only a third of the increment would be saved. Even, however, if this were so, it will be seen that the capital base on which plans for short-period productive schemes can be prepared would be considerably higher than at present postulated. It is certain that the rate of capital formation will rise steeply with production, and, therefore, a large amount of self-financing can be readily introduced into the assumptions of national plans.

A Rise by 50 Per Cent ?

In the case of India the Second Five-Year Plan now computed at an expenditure of Rs. 5,000 crores at the present prices, it would be appropriate to conclude that rupee finance raises no significant problem. Plans for other countries in South-East Asia will necessarily have to be less ambitious, running perhaps in proportions in correspondence with the figures in the Colombo Plan. But even so they would imply a rate of rise of 50 per cent in investment and something like a similar figure in industrial and agricultural production in the next six years.

Private Foreign Capital

The problem of private foreign capital is by no means so hopeful. In the statement below is evidence that no country of this area except Pakistan had a net inflow of private capital in the years 1948 to 1951. There is no reason to suppose, although private foreign capital will be welcome, that it is waiting to force an entry into any country in this area. It is best to consider private foreign capital as being a negligible factor of total investment in this area for some years to come.

**Net Inflow(+) or Outflow (—) of Private Capital (a)
In Specified Asian Countries**

(Millions of Current Dollars)

Country	1948	1949	1950	1951	Total
Burma	..	..	— 2.5	— 2.9	— 5.4
Ceylon (b)	+ 0.6	— 6.1	— 6.1	— 8.0	— 19.6
India	— 49.3	— 57.6	— 17.0	— 6.1	— 130.0
Indonesia	— 28.0	— 11.4	— 19.5	..	— 58.9
Pakistan (c)	+ 0.5	+ 2.5	— 0.1	+ 7.6	+ 10.5
Philippines	+ 26.0	— 13.0	— 65.5	+ 5.0	— 47.5

(a) Excluding amortization. Figures converted from nation currencies to U.S. dollars equivalent on the basis of conversion factors supplied by the International Monetary Fund.

(b) Relates to long-term capital only.

(c) Excluding transactions with India, Nepal and Tibet.

Foreign Aid

The contribution of foreign aid is happily not so negligible. It would seem clear because of military aid, which some countries in this area are already receiving from the United States, that dollar aid will not fall in the near future. Indeed, it will almost certainly rise, and it is conceivable that with economic aid added in, there might be a contribution of a billion dollars a year in the next five years. If that hope materialises, it would be legitimate to suppose that these resources could be appropriately shared, which would imply a great reduction of foreign exchange difficulties. In any case, the broad picture which arises from the conditions already mentioned is that the difficulties of finding the requisite capital are by no means as large as has been too frequently feared.

4. THE PROBLEM OF PAYMENTS

CLOSELY associated with the problem of capital in this area is the problem of payments. At the present time only India seems to have a fully stable favourable balance. The conditions of payments of the area have not always been unfavourable, and, as the table below shows, there are times when almost all the countries in the area have had favourable payments. The Korean boom was one of these. It is conceivable that a time may come when a similar boom will appear even as an element in a peace situation. This, however, is not likely and, therefore, the question arises as to how South-East Asia might finance its developments without embarrassment on foreign exchange account.

Balance of Payments (Current Account)
(£ Thousand)

Country	1951-52 (Actual)	1952-53 (Actual)	1953-54 (Estimated)
Burma	...	+13,379	- 0,375
Ceylon	...	-18,997	+ 615
India	-106,000	+48,000	+36,000
Indonesia*	+ 63,600	-65,200	-43,300
Malaya*	...	+ 3,700	-11,200
Sarawak*	...	+ 2,550	+ 150
Pakistan	-49,671	-43,918	- 3,065

*Calendar years.

A South-East Asian Payments Union

For some time past, there has been considerable discussion, largely academic, of a South-East Asian Payments Union. A Working Group of experts on payments problems met in Bangkok from the 19th to 28th July 1954 under the auspices

of the Economic Commission for Asia and the Far East. They came to the conclusion that the scope for additional multilateral compensation in ECAFE was limited. The quantum of additional trade which could be offset multilaterally through a payments union for the region was only 5 per cent of the total intra-regional trade in 1952 and 12 per cent in 1953. But it was pointed out that the European Payments Union (EPU) finances no larger a proportion of intra-regional trade, although EPU settlements include balances of payment outside Europe of the various monetary areas of EPU.

While there are advantages in setting up a Payments Union even for this small percentage of inter-regional trade which is not compensable, it would appear that a solution of the payments problem might be found not so much by a Union as by the making available of surpluses of one country for the purchases of another on mutually acceptable terms. For example, there is no reason why balances available with India in our Sterling Number One Account should not be used for short-term investments in Indonesia, Burma or Ceylon.

Wanted : A South-East Asian Bank of Development

This raises the question as to the best form in which investments should be provided as an element in production and loans as an element in a payments policy. Much the best manner in which the difficulties of payments in South-East Asia could be reduced is by the formulation of a common policy in these terms, and its implementation by a new Bank to be called the South-East Asian Bank for Reconstruction in which countries in South-East Asia could avail themselves of opportunities similar to those now available on a very limited scale through the World Bank. There is obviously scope for a new Bank to advance investment, and another which provides short-term funds to overcome payments difficulties. The South-East Asian Bank for Reconstruction can well undertake both functions. Its character may be similar, though obviously much more limited in purpose, to

those of the World Bank and the International Monetary Fund.

It is not necessary to set out the problem in additional detail. It would appear that in 1937, 70 per cent of intra-regional trade was bilaterally balanced, 9 per cent was multilaterally compensable, and 21 per cent represented either net surpluses or deficits which were not compensable on trade accounts within the region in the same year. The normal position now is less favourable and yet there is no reason to suppose that a pattern of trade could not be devised with the help of a suitable lending agency, to bring down the figure of trade not immediately compensable to 20 per cent of the total trade in this area. Indeed, in 1953, the percentage was back to 20 per cent.

For this purpose it is unlikely that the resources of the area will alone be sufficient and thus it will be necessary for this Bank to enter into an arrangement with the World Bank or with those governments whose currencies are in short supply.

5. INTER-REGIONAL TRADE AGREEMENTS

NOBODY need deceive himself on the marginal character of inter-regional trade agreements at the present time. They have merely put into writing, and in some cases ineffective writing, a pattern of trade normally taking place. In many cases, the full purposes of these agreements have not been realised, which implies both a change in demand and an unwillingness of the governments concerned to press hard for the spirit of the agreement where no specific quantity and price were entered.

It is obvious that if South-East Asia is to raise itself by its own bootstraps, inter-regional trade of this kind must be given far more understanding and implementation than it has hitherto had. On the side of the understanding must be considered the necessity of raising exports and imports back to their peak regional level. This cannot be done if countries in this area strive to become self-sufficient. In particular, India's self-sufficiency in rice is conceived in so insular a manner that it has done serious damage to the whole character of South-East Asian co-operation. A last minute decision to restore the purchase of rice from Burma has stopped the rot, but it will require far greater understanding to change the structure of thinking on national self-sufficiency and make it as much co-operation as possible for the whole.

Wanted, Machinery for Action

This, and nothing else, is the problem of South-East Asia's regional trade. At the present time, there is no body which has either the capacity to plan or the power to implement a programme of action conceived on regional lines. Certain clear evidence can, however, be given to indicate that