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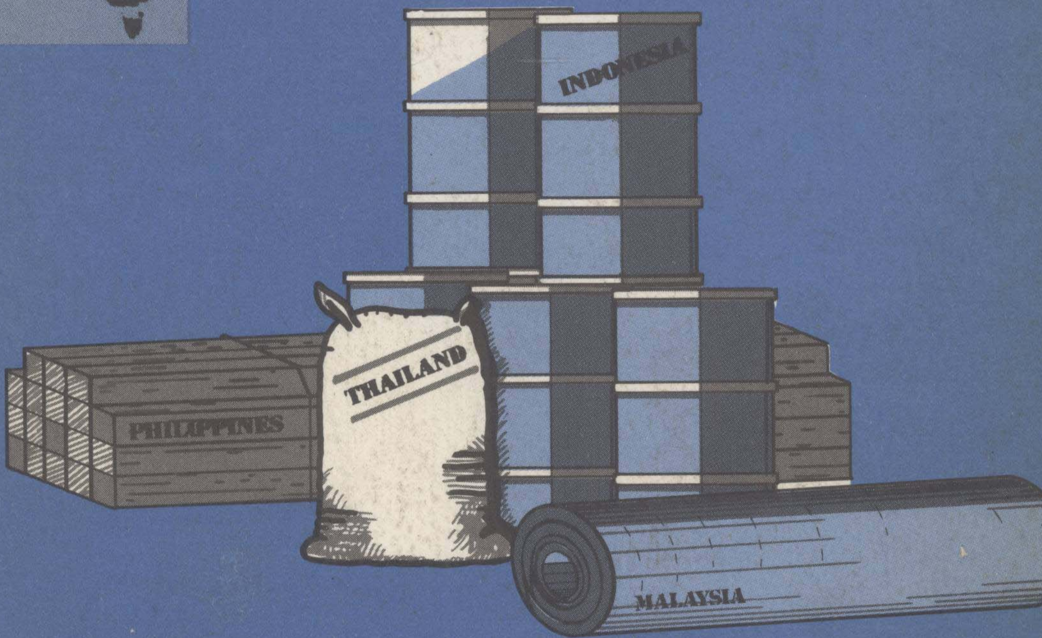
ASEAN'S 'other four': economic policy and economic performance since 1970

Bruce Glassburner



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Contents

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Introduction

The Association of Southeast Asian Nations (ASEAN) is now 16 years of age. The Association has received much deserved attention and praise for its achievements. Much of this success has been of a political nature; indeed, acting as an association, its successes fall almost exclusively in the political arena. This is not to say that economic success has eluded the five members individually. Quite the contrary. The combined (weighted average) real GDP per capita growth rate of the five members in the decade of the 1970s was 4.5 per cent — which, sustained, doubles in 16 years. Removing highly dynamic Singapore from the group makes little difference to that rate of growth because of its small population weight.

Singapore is being omitted from discussion in this paper, not because it is of less interest than the other four, but rather because it is such a special case. The larger four nations have more varied resources and are, very broadly speaking, more alike, and have more problems in common. Singapore, as one of the 'Gang of Four' or Asian 'NICs' (Newly Industrialising Countries) deserves a separate category. The 'other four' have done well economically, but significantly less well than Singapore; and they have, in varying degrees, more complex and less tractable problems of economic structure.

All of the 'other four' are now classified by the World Bank as being 'Middle Income Economies'. Until 1981, Indonesia was still categorised as one of the 'Low Income Economies', but its steady high per capita real income growth into the early 1980s has carried it past five nations since then. In general, all of the four except the Philippines[1] have outperformed the Middle Income category, as Table 1 shows.

The plan of this paper is simply to start at the top in Table 1, and proceed through the four, thus proceeding from the largest and poorest of them, Indonesia, to the smallest and richest of them, Malaysia. Indonesia is the appropriate starting place for two reasons. More than half of the total population of the group is found in Indonesia; hence the region can hardly succeed unless Indonesia succeeds. Beyond that, Indonesia is the country among the four which I know best; hence it is the appropriate point of departure for comparison for me. In each of these four brief country studies, the dimensions of policy orientation and economic performance that we will be most concerned with will be the following:

1. How 'outward looking' has the international trade and industrialisation policy been, and to what extent have those policies produced positive results?

[1]Whether the Philippines has done 'well' in this period depends on the point of reference. Although Philippine growth 1970-80 fell slightly below that of the average of all Middle Income Economies, it exceeded (marginally) the weighted average growth of the World Bank's newly defined 'Lower Middle Income economies' (see Table 1).

TABLE 1 Basic Data on ASEAN's 'Other Four'

Country	World Bank Rankings[a]	Population mid-1981 (million)	Population Density (pers./sq.km)	Population Growth 1970-81 (% p.a.)	GNP per capita 1981 (US$)	Growth of Real GDP per capita 1970-80[b] (% p.a.)	Annual Rate of Inflation 1970-81	Adult Literacy 1980 (%)	Life Expectancy at Birth 1981 (years)
Indonesia	41	150	78	2.3	530	4.8	20	62	54
Thailand	48	48	93	2.5	770	4.2	10	86	63
Philippines	49	50	165	2.7	790	3.5	13	75	63
Malaysia	77	14	43	2.5	1840	5.3	7	60	65
Low Income Countries	1-34	2210	71[d]	1.9	270	2.9[c]	11[d]	52[d]	58[d]
Middle Income Countries	35-94	1128	27[d]	2.4	1500	3.7[c]	13[d]	65[d]	60[d]

[a] Ranking among nations of the world according to 1980 GNP per capita from World Bank (1983a).

[b] GDP per capita in 1975 prices. This column was calculated from IMF (1982). All other data in this table are taken or calculated from World Bank (1983a).

[c] GNP growth 1960-81 from World Bank (1983a).

[d] Weighted average.

2. What were the repercussions of the 'oil shocks' of 1973-74, 1979-80, and 1982-83 on the economic system?
3. How has the nation handled its main macroeconomic policy instruments, that is, its budgetary and monetary policies?
4. How has the nation dealt with its agricultural sector, and how well has that sector performed?

These four areas of economic policy and performance are by no means separable in any clean fashion. However, they provide us with a manageable set of categories.

In the background of this sort of approach to a comparative study are the excitement and interest created by the very high growth peformance of Japan and the more recently emerged 'Gang of Four' of Taiwan, South Korea, Hong Kong, and Singapore, all characterised by extremely rapid growth of foreign trade — 'export-led growth'. The ASEAN 'other four' have also enjoyed high growth rates in the 1970s, and there is a natural inclination to assume that their growth, also, was due primarily to the adoption of 'outward-looking' policies, and that they may be regarded as the next 'Gang of Four'. But can they properly be so regarded? Or do they suffer from political and economic constraints that will stunt any such growth impetus?

It is not intended here to argue that an 'outward-looking' policy towards international trade is all that is required for development success; hence the four questions posed above. Resiliency in the face of uncertainty in both the domestic and international environment, good macroeconomic management, a supportive agricultural policy — along with reasonable stability in the political system — all can be crucial. The heavy emphasis on economic openness given here is rather intended to point up the high significance of meeting international standards of economic efficiency and of comparative advantage as a guide to resource allocation.

This paper, also, is not to be regarded as an argument for laissez faire. None of the four countries discussed can, even remotely, be considered a 'hands-off' government. Obviously, a strong trade orientation implies a relatively low level of intervention in the affairs of private enterprises engaged in international trade, and those producing tradeable goods. The essence of governmental responsibility in an open economic system is towards providing an environment for the efficient functioning of markets, which, to oversimplify, calls for supplying 'public goods' efficiently and in ample quantity. Such a government might well be large, particularly in a large economy, but its orientation will be more supportive than directive; it will allocate its resources so as to augment, rather than compete with, the private sector, except where there is a demonstrable social welfare case for more direct participation.

1

Indonesia

The Indonesian economy grew very rapidly in the 1970s and it is undeniable that its growth was 'export led' in the simple sense that exports grew faster than total output. It is much less appropriate, however, to describe Indonesian international trade and industrialisation policy as 'outward looking'. Even before the quadrupling of oil prices by the Organisation of Petroleum Exporting Countries (OPEC) in 1973-74, the economy under the Soeharto government had made rapid strides in expansion of exports. To be sure, much of this early rapid growth was recovery from the depths to which the Sukarno government had taken the economic system, and to some extent it was statistical illusion, created by the lifting of much of the maze of controls which the Sukarno government had imposed — and the resumption of much statistical reporting that had been forced into falsification by those controls.[2]

In the six years 1966-72, exports had increased in nominal US dollar value two and one-half times, and then increased another 79 per cent in the single year 1972-73.[3] The trade account balance was positive in both 1972 and 1973, although because of substantial services deficits, the current account balances remained negative (Rosendale, 1981; IMF, 1982). But both private and public capital inflows rose so rapidly that monetary movements, which had been virtually static or adverse, turned sharply in Indonesia's favour, with reserve accumulations of $610 million over the two years 1972 and 1973.

Balance of payments performance for the remainder of the decade held generally very strong, as indicated in Table 2. The rate of growth of exports was very impressive, with oil, of course, leaping ahead spectacularly over the six fiscal years from 1973-74 to 1979-80 at a compound rate

[2]Evasion of trade barriers is still prevalent in Indonesia through false invoicing, bribery of customs officials and smuggling. No recent efforts have been made to measure the magnitude of unrecorded trade which derives from these practices. For earlier efforts to deal with these problems, see Simkin (1970) and Richter (1970).

[3]Oil was the major contributor to this growth, jumping from $203 million to $913 million, 1966-72 (28 per cent per annum in US dollar value terms). Volume of oil exports rose by 17 per cent per annum. By comparison Arndt notes that real oil *output* growth had been 8 per cent per annum, 1950-66 (Arndt, 1983a). The US dollar value of non-oil exports also increased by 80 per cent, but rubber, once the proud mainstay of Indonesia's export bill, actually suffered a 15 per cent decline in value of exports, even though the unit value of rubber exports increased by 11 per cent over that period (IMF, 1983). This section draws heavily on my paper, 'Oil, Public Policy and Economic Performance: Indonesia in the 1970s' (Glassburner, 1983a).

TABLE 2 Indonesia's Balance of Payments, 1973/74 to 1982/83, actual (US$ million)

	1973/74	1974/75	1975/76	1976/77	1977/78	1978/79	1979/80	1980/81	1981/82	1982/83[a]
1. Net oil	**641**	**2638**	**3138**	**3710**	**4352**	**3785**	**6308**	**9345**	**13908**	**10429**
2. Net LNG[b]	—	—	—	—	**93**	**225**	**667**	**1256**	**n.a.**	**n.a.**
3. Non-oil (net)	**-1397**	**-2776**	**-3992**	**-4512**	**-5135**	**-5165**	**-4777**	**-8470**	**-16698**	**-17144**
Exports, f.o.b.	1905	2033	1873	2863	3507	3979	6171	5587	4170	3893
Imports, c.i.f.	-2938	-4341	-5090	-6167	-7241	-7543	-9028	-11837	-13228	-16457
Service (non-freight)	-364	-468	-755	-1208	-1401	-1601	-1920	-2220	-4850	-4580
4. Current account (1+2+3)	**-756**	**-138**	**-854**	**-802**	**-690**	**-1155**	**2198**	**2131**	**-2790**	**-6715**
5. SDRs	—	—	—	—	—	**64**	**65**	**62**	—	—
6. Official transfers ($ cap.)	**643**	**660**	**1995**	**1823**	**2106**	**2101**	**2503**	**2529**	**2712**	**3772**
IGGI	556	513	945	1596	1694	1625	2050	2251	n.a.	n.a.
Program aid	281	180	74	147	157	94	239	118	n.a.	n.a.
Project aid	275	333	871	1449	1537	1531	1891	2411	n.a.	n.a.
ODA	275	333	482	513	661	814	919	1144	n.a.	n.a.
Non-ODA	—	—	389	936	876	659	892	989	n.a.	n.a.
Non-IGGI	87	147	1	227	412	534	453	278	n.a.	n.a.
Cash loan	—	—	1049	—	—	—	—	—	n.a.	n.a.
7. Debt repayment (principal)	**-81**	**-89**	**-77**	**-166**	**-761**	**-632**	**-692**	**-615**	**n.a.**	**n.a.**
8. Miscellaneous capital	**549**	**-131**	**-1075**	**38**	**176**	**392**	**-1315**	**-361**	**1140**	**1397**
Direct investment	331	538	454	287	285	271	217	140	n.a.	n.a.
Oil sector	18	13	14	-32	-50	75	-1240	685	n.a.	n.a.
Other	200	-682	-1543	-217	-59	196	-292	184	n.a.	n.a.
9. Total (4 to 8)	**355**	**302**	**-11**	**893**	**831**	**770**	**2759**	**3746**	**1062**	**-1546**
10. Errors and omissions	**5**	**-311**	**-353**	**108**	**-180**	**-62**	**-1067**	**-1010**	**-2050**	**-1734**
11. Monetary movements	**-360**	**9**	**364**	**-1001**	**-651**	**-708**	**-1692**	**-2736**	**988**	**3280**

[a] Preliminary.

[b] Gross exports of products less imports of goods and services of the oil and liquified natural gas (LNG) sectors respectively.

Source: Bank Indonesia. Data for 1981/82 and 1982/83 derived from Bank Indonesia, *Indonesian Financial Statistics*, May 1983 — categories not strictly comparable to earlier years.

of 46 per cent per annum in nominal US dollar terms. But the growth of non-oil exports was also very rapid — 21.6 per cent per annum (US dollar value) over the same period of time. However, the current account remained negative until the final fiscal year of the decade of the 1970s since imports grew at virtually the same rate as non-oil exports, that is at 20.6 per cent per annum, while the services account remained heavily negative.[4]

That exports led output growth in Indonesia is thus not to be questioned. In 1967, the year of ASEAN's formation, and, essentially, the first year of the Soeharto government's new economic policy, exports represented 8.8 per cent of gross national product; whereas in 1981 they accounted for 27.5 per cent of GNP.

But it is necessary in judging the Indonesian case to recognise that external forces were extremely important, and that trade policy retained basic shortcomings that make it unlikely that ASEAN's largest nation can sustain this source of growth impetus for the future, unless basic attitudes and policies can be adjusted. The first point to be made is that the terms of trade improved hugely during the period 1972-80. The barter terms of trade ratio (1973 = 100) leaped from 72 to 291. The tenfold increase in the price of oil was largely responsible for this, of course, but non-oil prices also moved strongly with a rate of increase of the weighted average of the prices of the six most important non-oil commodities of 26 per cent per annum over the seven year period from 1972-73 to 1979-80.[5]

Thus it was *not* a great triumph of trade liberalisation that brought on Indonesia's rapid export growth and its strong foreign exchange position,[6] but primarily a matter of very good fortune in the terms of trade across a broad spectrum of traded goods, combined with a large, sustained official capital inflow. Foreign aid grew faster than non-oil exports; while net non-official capital inflows were actually negative over the period 1973-74 to 1979-80. Indonesia's official external debt, although high, has not become dangerous in spite of this pattern of capital flow. Total disbursed debt had reached $19.7 billion at the end of 1982, roughly 20 per cent of gross domestic product. Debt service for fiscal year 1982-83 is estimated at 22 per cent of export earnings (World Bank, 1983b).

[4]This is not to suggest that current account balance is inherently 'good'. A current account deficit supported by a manageable rate of capital inflow, and imports rising *pari passu* with export earnings are normal aspects of healthy growth.

[5]The six are timber, rubber, coffee, tin, palm oil, and copper. Weights used are 1979/80 export value. In the following two years, these prices fell by 12 per cent. Calculated from World Bank (1983b, Appendix Table 3.2).

[6]Gross reserves reached $6.8 billion by 1980, but had fallen to $3.0 billion by March 1983, when the devaluation apparently succeeded in reversing the capital outflow (Glassburner, 1983b).

To give credit where due, progress was made by the Soeharto government in dismantling the stifling, unenforceable network of controls on trade which they inherited from the 'Old Order'. This was particularly true of the foreign exchange system. From a multi-tiered exchange regime of unfathomable complexity in 1967, the Soeharto government moved to a unified, convertible exchange system in 1969. Exchange control from that point onward has been indirect, that is, by means of intervention in the foreign exchange bourse by Bank Indonesia as buyer or seller, as the situation seemed to require. In addition, attempts were made to simplify procedures at the major ports, to eliminate most of the 'unofficial taxes' on trade, to lift the majority of the formal export taxes, and to simplify the tariff structure. They have come far, but they have not come far enough if they are to hope to resume and sustain rapid growth in the future.

Why this pessimism about a regime that has come so far, so fast? Space does not allow for a full analysis of all aspects of the policy pattern, but the essentials are as follows: the industrialisation strategy, upon which the long-term future of export-led growth must depend has been, and remains, primarily import substitution-oriented. Protection levels, despite the 1973 tariff reform, remain extremely high, and probably mask low or even negative value-added within very high rates of growth of industrial output as measured in domestic prices (Boediono, 1983; Gray, 1982). The combination of periods of nominal exchange rate stabilisation and rapidly growing domestic government expenditure have combined to weaken the competitive position of Indonesian exporters in international markets despite periodic large (and therefore disruptive) devaluations. The generally distrustful attitude towards private entrepreneurship, and the consequent reliance on government investment to increase industrial output have inhibited private investment, and prevented the kind of self-propelled export-led growth that is characteristic of the 'Gang of Four'. And, finally, despite all efforts so far, the bureaucratic snarls associated with investment and trade remain deeply entrenched and intractable (see McCawley, 1980, for a similar view).

The impact of the first two 'oil shocks' of the 1970s on the Indonesian economy was favourable, because Indonesia is an oil exporter of significance. The oil glut of the early 1980s has had comparable depressing effects. In all three cases, radical changes in oil prices have forced adjustment problems on Indonesian policymakers. In 1973-74 and 1979-80, the essential problem was one of coping with the surge of foreign exchange availability. Its most important impact, of course, was the alleviation of the foreign exchange constraint, which allowed rapid expansion of both investment and consumption, and for a build-up of foreign exchange reserves. However, it also created a problem of monetary and fiscal management, and one of exchange rate policy. Government revenues (largely derived from oil company taxes) increased at a very rapid rate, providing the incentive for equally rapid increases in government expenditures. However, oil company revenues are collected almost entirely in US dollar terms; hence, unless expatriated or utilised for the import of goods, they must be converted into Indonesian currency at Bank Indonesia. Indeed, it is via this process that Bank Indonesia accumulated reserves. Thus, the Indonesian budget, although always nominally balanced, was expansionary, and led to quite rapid rates of monetary growth, and an internal rate of inflation higher than that of Indonesia's trading partners.

A concomitant of this problem was that the Indonesian rupiah has continuously declined in relative purchasing power. However, Bank Indonesia maintained a stable nominal rate of exchange against the US dollar over extended periods (for example, the rate was fixed at $1 = Rp 415 from 1971 until November 1978), with the result that Indonesian producers of import-competing and exportable goods were placed at a competitive disadvantage — or, as the international economists say, the 'real effective exchange rate' appreciated (by about 40 per cent over the period 1971-78). It was concern over this difficulty that led to the 34 per cent devaluation in November 1978. The latter decision was undertaken under the assumption that Indonesia's export earnings and public revenues would soon be slackening off in the face of a declining real price of oil on international markets, and a rapidly rising rate of domestic consumption of oil products. The Indonesian government did not anticipate that OPEC would undertake another round of radical price increases in another year's time. Although the 1978 devaluation was a success in the sense that it was followed by a surge of non-oil exports,[7] it exacerbated inflationary tendencies, and was then overwhelmed by the new surge of foreign exchange earnings as OPEC again doubled prices in 1979-80.

The same problems of monetary and reserve management had to be faced once again, and this time the Indonesian authorities allowed the nominal rate of exchange against the US dollar to float upward slowly — roughly at the rate at which the US dollar was appreciating against the SDR. The oil glut brought on by the world recession of 1982-83 has brought yet another type of shock to Indonesia in the form of a sharp drop in official prices of oil (17 per cent), and an even sharper drop in volume of oil production and sales. The balance of payments plunged to a current account deficit of $6.7 billion for fiscal year 1982-83, and the drop in government revenues has led to severe retrenchment (McCawley, 1983; Glassburner, 1983b). As a first major step by the Fourth Development Cabinet to meet this crisis, Indonesia devalued again, by 27.5 per cent, on 30 March 1983. A series of dramatic investment rescheduling announcements has followed, and in June 1983 a major reform of banking regulations was undertaken. A major reform of the taxation system is

[7]As Garnaut (1979) has pointed out, non-oil export growth was under way *before* the 1978 devaluation, and the extent to which the devaluation contributed to the surge is difficult to assess.

expected before the beginning of the Fourth Five Year Plan in April 1984 (Arndt, 1983b; Awanohara and Habir, 1983; Glassburner,1983b).

Most of what needs to be said about Indonesian macroeconomic policy is implicit in what has preceded, inasmuch as it is inextricably interwoven with balance of payments policy. Budgetary policy has been nominally conservative, in that all budgets of the Soeharto government have been 'balanced'. This so-called balance, however, is achieved by accounting foreign aid proceeds as receipts and by hiding domestic deficits and surpluses in accounts with Bank Indonesia. Moreover, as already indicated, the monetisation (in rupiah terms) of dollar-denominated revenues has made government finance expansionary. Thus the money supply, narrowly defined, increased at 32 per cent per annum from 1971 to 1982. With such rapid money growth, it is surprising that the average rate of inflation (1971-81) was no more than 17 per cent (Jakarta cost of living index). It implies a great deal of absorption of real money holdings (nearly 7 per cent per annum).

The government budget quadrupled in real terms (on the expenditure side) between fiscal year 1972-73 and 1980-81 — starting, of course, from a very low base. As a share of GNP, government expenditure rose from 14.0 per cent in 1970 to 26.5 per cent in 1980. The largest part of this growth was financed by rapidly rising oil revenues, but the commonly held notion that the availability of oil income weakened the government's effort at non-oil tax collection is not borne out by examination of the revenue data, except for the notably weak revenue buoyancy of the personal income tax (Glassburner,1983a).[8] While non-oil tax receipts remain low as a proportion of GDP, they have grown rapidly enough to prevent a fall in that proportion. The forthcoming tax reform is designed to increase it.

Banking, credit, and interest rate policies were of mixed quality. Capital rationing and interest subsidies have been constant, and have contributed to capital intensification, particularly in government investment; but interest rates to that part of the private sector lacking access to preferential lending, and to savers, were usually positive in real terms, and contributed to the monetary absorption referred to above. The private banking sector is not well developed, despite rapid growth of private banking in recent years, because of the limitations placed on foreign and non-indigenous bankers. State-owned banks have thus been allowed to dominate commercial banking, and they have been heavily favoured by subsidised liquidity credits from the Central Bank. Credit control of the

[8]This is not a trivial flaw. Indirect taxation of private incomes should be expected to grow relative to other forms of government revenue, provided the income tax law is reasonably well designed and enforced. While the Soeharto government has improved taxation performance generally, reform and enforcement of the poorly designed and still more poorly enforced personal income tax has been deferred. A streamlined tax law and enforcement system is expected in early 1984 as part of the tax reform package mentioned above.