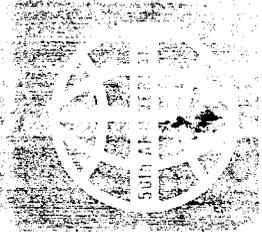


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THE EVOLVING ROLE OF THE WORLD BANK

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The East Asian Economic Miracle

The Evolving Role of the World Bank

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Vinod Thomas and Peter Stephens

**The World Bank
Washington, DC**

The World Bank Group

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The World Bank Group today includes five international organizations:

The International Bank for Reconstruction and Development (IBRD), the original institution in the group, opened its doors for business in 1946. Today, it is the largest source of market-based loans to developing countries and is a major catalyst of similar financing from other sources. It lends to governments or to public or private entities with government guarantees. It is funded mainly through borrowings on the international capital markets.

The International Finance Corporation (IFC) was established in 1956 to support private enterprise in the developing world through the provision and mobilization of loan and equity financing and through its advisory activities relating to, among other things, capital market development and privatization. IFC is also a major catalyst of both local and foreign private investment. Its lending and equity investment activities are based on the principle of taking market risk along with private investors. Under the terms of its Articles of Agreement, it cannot accept government guarantees.

The International Development Association (IDA) was created in 1960 to provide finance on concessional terms to low-income countries that lack creditworthiness for IBRD borrowing. IDA is primarily funded from grants it receives from donors in periodic replenishments.

The International Centre for Settlement of Investment Disputes (ICSID) was added to the World Bank family in 1966 to provide conciliation and arbitration services for disputes between foreign investors and host governments that arise directly out of an investment.

The Multilateral Investment Guarantee Agency (MIGA) was created in 1988 to provide noncommercial investment risk insurance and technical services that help promote investment flows. It also disseminates information on investment opportunities.

As is now common practice, the "World Bank" or simply the "Bank" are used interchangeably to mean both IBRD and IDA. The "World Bank Group" refers to IBRD, IDA, IFC, ICSID, and MIGA.

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Foreword

The world has changed dramatically over the last five decades and so has the World Bank. The Fiftieth Anniversary of the World Bank has provided us with an opportunity to reflect on and learn from the Bank's experience and to apply the lessons to the Bank's future agenda.

This series of essays is devoted to improving understanding of the evolving role of the World Bank. Each essay analyzes the Bank's approach to the major development challenges its borrowing countries have faced, starting with the reconstruction and development needs of Europe and Japan in the 1940s and 1950s and ending with the transition of Central and Eastern Europe and the former Soviet Union. One essay examines the evolution of the Bank's relations with the world's capital markets as it mobilizes private savings for development. An overview paper provides a picture of the fifty-year period as a whole.

The story that emerges is one of an evolving and learning institution that has built on its successes and its mistakes. The Bank has responded with vigor and energy to the challenges confronting its borrowers. In this process, it has made a significant contribution to the impressive developmental gains recorded in these past fifty years. In responding to those challenges, the Bank itself has changed, learning from its experiences, deepening its understanding of the development process, and recasting its analytical and financial support to help its borrowers better.

The Bank will continue to nurture its tradition of self-evaluation and learning. These essays will, I hope, contribute to a better-informed debate on the Bank's future role. They complement the recently issued paper, *The World Bank Group—Learning from the Past, Embracing the Future*, which sets out the future directions for the Bank Group.

Armeane M. Choksi
Vice President, Human Resources Development and Operations Policy, and
Chairman of the Bank Group Committee on the 50th Anniversary

The East Asian Economic Miracle

Vinod Thomas and Peter Stephens

East Asia has been uniquely successful in fostering growth, reducing poverty, raising living standards, and integrating with world markets. The credit for this remarkable achievement belongs to the governments and peoples of the region. They were not alone, however. Open markets in industrial countries and development assistance contributed to progress. Since its first loan to Thailand in 1950, the World Bank has had a long and active involvement in the region—in lending some \$71 billion through fiscal 1994, and in policy dialogue (see Figure 1).

With remarkable commitment and perseverance, East Asia has practiced the key messages emphasized by the Bank in its development strategy: macroeconomic stability, investment in people, and building on export growth. The impact of the Bank's involvement is not easily defined in monetary or economic terms; it is better understood through the diversity and continuity of the relationship with its East Asian member nations.

It is a mature relationship, and there have been differences along the way. For example, the Bank and its member countries have, at times, differed on the allocation of resources across the spectrum of social and infrastructural services, or on the appropriate

East Asia has been uniquely successful in fostering growth, reducing poverty, raising living standards, and integrating with world markets

timing of a switch in industry policy. And this is as it should be: the Bank's advice and recommendations are just part of the menu of options countries may choose from in managing their development.

And though the region is the fastest growing, East Asia's record is not unblemished. Not all countries have sustained high rates of growth. East Asian governments have not always given adequate attention to such crucial issues as protection of the environment and investment in infrastructure, which have too often lagged behind rapid economic expansion. Much

has been achieved in East Asia, but much remains to be done.

Diversity and Commonality

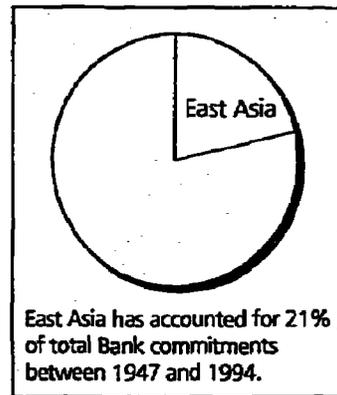
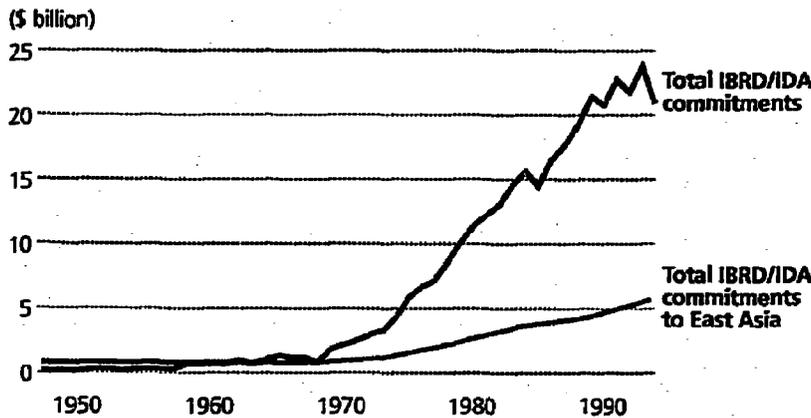
East Asian economies are remarkably diverse. The region includes some of the richest developing nations—such as Korea, and some of the poorest—such as Vietnam. It includes the world's most populous country, China, as well as one of the least populated, Laos. Some countries, like Malaysia, have a store of natural resources, while Korea has virtually none.

No single development formula lies behind the "East Asian

Much has been achieved in East Asia, but much remains to be done

Figure 1. IBRD and IDA Commitments, 1950-94

World Bank commitments to East Asia totalled over US \$6 billion in 1994



miracle," and the Bank has not adopted a single development template. The sheer size and cultural diversity of a region that is home to 1.67 billion people—about one-third of the world's population and about 20 percent of its poor—provides a wide variety of development challenges and attendant development problems—including environmental degradation, infrastructural bottlenecks, and poverty.

Such problems notwithstanding, today, rapid economic development is a common feature of much of East Asia. There has been a near quadrupling of per capita incomes in the past twenty-five years, a marked improvement in health and education, a decline in fertility, and a surge in agricultural and industrial output. Outward-oriented East Asian economies have integrated with the global economy to a remarkable extent, and have emerged as the driving force behind global trade growth. Perhaps most important, economic growth has not only been dramatic, it has been broad-based and, on the whole, equitably distributed.

Why has East Asia, with its diverse economies and problems, been so successful? There is no simple answer. Policy approaches by East Asian economies have also been diverse. The first generation of newly industrialized economies—with the exception of Hong Kong—opted for relatively more state intervention, as had Japan earlier on. Among the second generation, Indonesia and Malaysia had little success with early interventions. Less interventionist over the past dozen years, they both achieved markedly better economic performance. Most recently, newly industrializing economies and areas such as Thailand and coastal China, have been inclined to less extensive intervention.

Behind country variations, however, are significant common features. One such factor is human resource development. In this respect, strong public policies were augmented with high household investments in education in most countries.

Investment in people is closely linked to the notion of equity

Outward-oriented East Asian economies have integrated with the global economy to a remarkable extent, and have emerged as the driving force behind global trade growth

with growth. Some economies, such as Korea, brought about an early and relatively equitable distribution of land. These countries, and others (including, for example, Malaysia) continued to ensure that a majority of the population shared the benefits of economic growth in a variety of ways. The result was a striking decline in absolute poverty, which is illustrated most dramatically in Indonesia.

Common to East Asia's success were policies for participation in world markets and macroeconomic stability. Because the economies took international prices as a primary guide to domestic resource allocation, macroeconomic stability was seen as central to maintenance of international competitiveness. Moreover, most governments had a strong aversion to inflation, which strengthened the hands of technocrats. Where external or internal factors threatened overall equilibrium, governments moved quickly and credibly to restore stability.

At the core of development success in East Asia has been pragmatic policymaking, from

policy design to effective implementation. Pragmatism means the relative absence of ideology in setting policy and the willingness and ability to change failed policies. Socialist economies in transition illustrate both the costs of ideology and the gains to be made from changing course. China's reform program has been little short of breathtaking.

The sections that follow are devoted to one important aspect of the Bank's involvement in each of the six countries in the region that accounted for 95 percent of the Bank's lending to East Asia (see Figure 2).

Investing in People in Korea

In the 1960s, when the Bank's involvement in the region began in earnest, East Asia's people placed high value on education, which was reflected in public and private spending. In later years, educational investments have provided universal primary education and widely available secondary education.

At the core of development success in East Asia has been pragmatic policymaking, from policy design to effective implementation. Pragmatism means the relative absence of ideology in setting policy and the willingness to change failed policies

Education was revered not only for its own sake but as a means of achieving economic development. Equally important was the emphasis on strong human resources in government, which complemented the prevalent ethic of public service in East Asia. This provided fertile ground for the Bank's emphasis on human resource development.

Witness Korea. In just one generation, Korea has left the ranks of those qualifying for World Bank loans. (Korea received its first IDA credit in 1962 and its first IBRD loan in 1968. By 1992, per capita

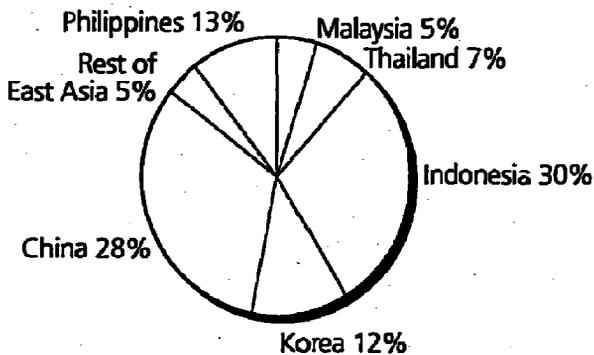
income had reached \$6,790, and by 1995 it will have graduated fully from Bank lending.)

From the 1960s, successive Korean governments invested heavily and effectively in primary, secondary, and high-school education. Korea's program involved heavy investments in physical facilities. In 1960-70, the number of primary schools increased from 4,496 to 5,961, and middle schools from 1,053 to 1,608. By 1989, they had reached 6,396 and 2,450, respectively. The number of high schools also expanded from 640 in 1960 to 1,672 by

In just one generation, Korea has left the ranks of those qualifying for World Bank loans

Figure 2. IBRD and IDA lending to East Asia by major recipient, 1950-94

Indonesia and China received the largest share of the US \$71 billion lent to East Asia



In Korea, adult literacy reached 92 percent by 1985 and is almost 100 percent today

1989. Government financial support at the primary level also extended to targeted subsidies for items such as school meals and uniforms. Government education expenditures rose from 2.6 percent of GNP in 1960 to 3.4 percent in 1989, while—as a proportion of government expenditures—the allocation for education rose from 11 percent to almost 20 percent.

The impact on school enrollment was dramatic. By 1970, Korea had 100 percent enrollment in primary education, while between 1970 and 1989, those enrolled in middle schools grew from 57 to 99.7 percent of all school-age children. High school enrollment rose from 30.5 percent in 1970 to 78 percent by 1985. Along with population expansion, this meant that the number of primary school students in Korea increased from nearly 3.6 million in 1960 to 4.9 million in 1989. Middle school students rose from 530,000 to almost 2.4 million, while high school students increased from 273,000 to 2.3 million. The number of teachers also increased sharply

in 1960–89, with the ratio of primary school students per teacher falling from 59 to 36, and for middle school students, from 40 to 29.

Korea's aim was two-fold: to achieve a high literacy rate and, by emphasizing technical skills, to create a well-educated work force capable of meeting the challenge of rapid and technology-based economic development. Korea succeeded on both counts. Adult literacy (and numeracy) reached 92 percent by 1985 and is almost 100 percent today. Since the 1960s, a large pool of educated labor, including many women, has helped underpin Korea's industry-intensive and export-oriented development drive.

Past Bank lending focused on strengthening science and technical education to underpin Korea's ambitious plans for industrialization. In the 1970s, lending was mainly for expansion and quality improvement of vocational and technical education in high schools, junior technical colleges, and undergraduate programs in science and engineering. In the early 1980s, emphasis was

placed on improving policy with the aid of two education sector loans, which led to institutional improvements in such areas as evaluation and accreditation, personnel planning, equipment maintenance, curriculum development, and private education. These efforts were reinforced by the Sector Survey of Science Education (1982) which set a long-term strategy for strengthening science education at the secondary and higher levels.

As Korea's industrial sector moved toward higher value-added, technology-intensive production, the government placed greater importance on strengthening local capacity for research and innovation. In response, Bank lending shifted its emphasis in the late 1980s toward strengthening graduate schools of science and engineering (which train research personnel) and directly supporting selected national research institutes.

In some recent projects, the Bank has also focused on strengthening environmental science and technology in universities and research

institutes, in line with the government's increasing concern about environmental problems. The Bank has also continued lending for vocational and technical education to ensure that training of craftsmen and technicians keeps pace with rapid technological change in industry. A continued interest in supporting policy improvements is reflected in the last Bank education loan to Korea (1994). This includes a range of institutional improvements in secondary and higher science and technical education. Building on previous changes, these are expected to help guide policies over the next decade.

Over the past quarter century, the Bank made sixteen education loans totaling \$906 million (and with total project costs of almost \$2.6 billion). Lending has, in general, been consistent with Korea's needs and priorities in science and technical education and has paralleled the increasing sophistication of its industry. There was early recognition that the restructuring of industry toward skill-intensive, high technology production

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In addition to helping Korea, the Bank learned much about forming workable policies to increase the quality and relevance of education and research

would require continuous upgrading of Korea's skill base. Bank lending matched this change in demand. But, in addition to helping Korea, the Bank learned much about forming workable policies to increase the quality and relevance of education and research. It also learned lessons on practical issues (such as mechanisms for curricular change and the preparation of equipment lists) relevant to a range of institutional, teaching, and research objectives. These lessons are now benefiting the design of projects in Thailand, Indonesia, and Malaysia.

Human resource development is still a major challenge in East Asia. Problems concern not only the provision of basic education in low income economies but also the provision of adequate secondary and higher education and the adequacy and quality of all education. With the region committed to international markets, it is crucial that the educational system be flexible enough to respond to needs of skill formation so that countries remain competitive. The Bank continues to be a key player in

facilitating financing and provision of best practices in human resource development in East Asia. This role is likely to assume even greater significance in the years ahead, as countries of the region continue to grow and become ever more competitive.

Reducing Poverty in Indonesia

An education policy aimed at broadening the base of the work force enables wider participation in the fruits of national growth, and can contribute significantly to poverty reduction and social equity. But poverty must also be addressed through other policy instruments. Here the East Asian record has been particularly impressive. As a result of rapid economic growth and a multi-faceted development approach, involving human resource development and the provision of basic physical infrastructure, absolute poverty in the region has declined by around two-thirds during the past twenty-five years.

The number of absolute poor in East Asia is estimated to have fallen from 400 million in

1970, to 300 million in 1980, to 180 million by 1990.¹ This is all the more remarkable given that the region's population has expanded by some 425 million over the past twenty years. Moreover, reducing poverty to little more than one-tenth of the region's population contrasts sharply with the experience of other developing regions. In 1990, the absolute poor still accounted for roughly half the population in South Asia and Africa and one quarter in Latin America. How did East Asia manage to reduce poverty to such an extent?

Indonesia is a good example. Twenty years ago, Indonesia was among the poorest countries of the world, with a per capita income much less than that of India, Bangladesh, and Nigeria. Today, Indonesia's GNP per head has reached \$670, and those living in absolute poverty have dropped from around 70 million (60 percent of the population) at the beginning of the 1970s to near 27 million by 1990 (about 15 percent). This is the fastest rate of decline in poverty in any country, and it coincided with enormous

improvements in nutrition, life expectancy, basic schooling, and health of the poor.

Three key reasons led to the progress of Indonesia's poor:

- Rapid economic growth generated strong growth in demand for labor (and so, in incomes), first in rural areas, and later in cities.
- Relatively free labor markets allowed workers to migrate to jobs, especially from rural to urban areas.
- Basic infrastructure, health, education, and family planning services were expanded and made accessible to most of the population, raising productivity and the quality of life, and breaking down barriers to the movement of goods and people.

Indonesia has achieved sustained and high economic growth, averaging more than 6 percent a year in 1970-90. More important, this growth was broadly based, spreading its benefits to even the poorest. This was because:

The number of absolute poor in East Asia is estimated to have fallen from 400 million in 1970, to 300 million in 1980, to 180 million by 1990

- The government placed emphasis on improving the agriculture sector, on which the livelihood of most people, especially the poor, depended.
- The shift to rapid industrial growth in the mid-1980s emphasized a more labor-intensive, outward-oriented path of industrialization.
- These two growth processes created new service jobs in non-farm activities and urban trade, construction, and finance.

One central reason why so many poor people were able to raise living standards was that the great increase in job opportunities coincided with slower growth in labor supply. Indonesia had been successful in reducing fertility and in providing basic education and health to the population. Reducing the growth of the labor force and increasing its quality, perhaps more than any single factor, lies behind Indonesia's sustained decline in poverty.

Many of the dramatic gains in human capital came as a result of government decisions to

provide education, health, family planning, and other social services nationwide. Special programs (the INPRES, or Presidential Instruction, programs) covered the countryside with roads, primary schools, and public health facilities. Between 1978 and 1987, primary school enrollments among the poorest 40 percent rose from 78 percent to 90 percent; lower secondary enrollments rose from 42 to 65 percent; and the utilization of health services doubled (though it remains low).

In the 1980s, Indonesia even managed to reduce poverty, in both relative and absolute terms, at a time of difficult adjustment to external shocks. External strains severely affected the economy, creating the need for two rounds of adjustment—in 1982–85 and again in 1985–88. These strains included a sharp decline in the terms of trade, falling oil prices, and an appreciation of the U.S. dollar, which then increased Indonesia's external debt burden. Adjustment involved significant devaluation of the rupiah, reductions in public

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expenditure, and comprehensive tax, trade, and financial reforms. Some of these continue to be key challenges ahead.

Indonesia's attack on poverty, however, predates the adjustment period of the 1980s. In the 1970s and early 1980s, it made use of buoyant oil revenues to finance rural infrastructure (such as irrigation facilities, rural electrification, and roads for transporting produce to market) and to provide fertilizer subsidies. This was in marked contrast to the experience of other oil-exporting countries of the region. Though much of the initiative behind these programs was Indonesia's, the Bank was heavily involved in certain areas, such as irrigation. (The Bank has been prepared to throw its weight behind policies proposed by able technocrats—Indonesia's included—to help counter political and other vested interests ranged against economic reform. In the case of Indonesia's attack on poverty, however, the decision to protect rural groups found support at the highest political level.)

Indonesia still faces daunting problems, but why was the country able to avoid or overcome some of the problems encountered in other countries over this period? Credit goes to a clearly articulated long-term vision of development, an able economic team given considerable freedom to make decisions, a desire for macroeconomic stability, and a realization of the importance of the agricultural sector for economic growth and poverty reduction.

The World Bank played a supportive and vital role, providing timely and relevant economic advice and substantial financing for Indonesia's public investment program in education, health, agriculture, and infrastructure. The Bank's policy advice intensified during the crucial years of adjustment—the 1980s—on major macroeconomic reforms. It encouraged development of labor-intensive manufacturing industries, as an alternative to commodity exports, to absorb labor that might otherwise have entered the ranks of the poor. These reforms (backed by three World Bank structural adjustment loans) were effective

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East Asia's excellent inflation record is largely the result of sound fiscal policies and budgetary discipline

because the government was committed to them. It implemented reforms quickly and consistently and took ownership of the reform agenda, adapting it to suit the country's needs and priorities.

But while East Asia has had great success in reducing poverty, the region still has a large share of the world's poor. The task of poverty reduction remains daunting. Increasingly, the challenge is to reach the so-called "hard-core" poor, which requires sustained economic growth as well as human resource development and targeted poverty programs.

Macroeconomic Stability in Malaysia and Thailand

Almost universally, successful East Asian economies have adhered to sound macroeconomic policies. Steady economic growth and low inflation have provided a stable framework for long-term planning and encouraged saving, investment, and the efficient deployment of resources. At the same time, exchange rates have generally not been overvalued in real terms. From the 1970s

onward, East Asian inflation averaged half that of other lower-middle-income countries. Real interest rates averaged a positive 4 percent (compared with a negative 3 percent elsewhere) ensuring a good return on savings and setting a clear benchmark for the cost of capital.

East Asia's excellent inflation record is largely the result of sound fiscal policies and budgetary discipline. Over the past twenty-five years, the region's fiscal and current account deficits averaged less than half those of other developing countries. Macroeconomic management also gained from generally strong and prudent central banking institutions.

While East Asian countries have not completely avoided macroeconomic difficulties, they have usually reacted more quickly, and often adjusted less painfully, than have other developing countries. In both Malaysia and Thailand, for instance, the central bank tends to be the most powerful economic agency and has a strong preoccupation with controlling inflation. But even

a conservative macroeconomic policy managed by able technocrats cannot insulate an economy against external shocks. Between 1980 and 1985, following the second oil shock and a general decline in commodity prices, Thailand came under severe financial strain, particularly on its external account. Malaysia also suffered severely, and at a time when heavy investments in capital-intensive industries were absorbing a large part of national resources.

But following the second oil shock—which revealed structural weaknesses in the country's balance of payments—Thailand adopted a strong adjustment program. The government redesigned its trade and industrial policies to offset the bias against exports. Tariffs were rationalized and average rates reduced (though effective protection rates for manufacturing remained significantly higher than in other East Asian countries). At the same time, the Board of Investments adopted foreign-exchange generation as a criterion for approving inward investments, thereby stressing

export activities. The new outward orientation was supported by other policies, including a significant depreciation of the baht, tax exemptions for exporters, and the setting up of export-processing zones.

In the 1980s, when inflation and other macroeconomic variables were threatening to get out of hand, the Bank was called upon to intervene more directly. It provided Thailand with its first structural adjustment loan (\$150 million) in 1982 and a second one (\$175 million) in 1983. Subsequently, the Thai economy weathered the crisis: current account and fiscal deficits improved despite significantly higher world real interest rates, weaker export demand, and less favorable terms of trade.

The consensus among Thai government officials and Bank staff was that Bank involvement had made a real difference in helping to solve the country's problems. Here, too, the Bank's involvement can be said to have been cooperative with the government and responsive to concerns that were identified early on in

Even a conservative macroeconomic policy managed by able technocrats cannot insulate an economy against external shocks

what proved to be a protracted period of macroeconomic stress.

Bank support through structural adjustment loans had advantages. First, by underwriting a broad structural adjustment program, the Bank strengthened the domestic and external credibility of the effort and helped to maintain its momentum. Second, by working with the Thai government on the program supported by the loans, the Bank helped translate the structural adjustment strategy into policies and speed their implementation. Third, by including policy measures under structural adjustment lending, the Bank helped focus and supervise related technical assistance activities.

In Malaysia's case, the Bank was asked to augment its traditional support for projects with greater involvement in macroeconomic adjustment. By 1985-87 the international price of oil had virtually halved, and Malaysia's heavy industry was absorbing a large part of the nation's investment resources. The seeds of this

problem had been sown in the early 1980s, when frustration with the pace of economic development in Malaysia prompted a state-led drive to upgrade industry. This was buttressed by an increase in oil and gas revenues. By 1981, public expenditure had reached 58.4 percent of GDP, as Malaysia invested in a range of capital-intensive manufacturing activities—mainly through the Heavy Industries Corporation of Malaysia. But by 1988, the inefficiencies associated with this drive became evident when a set of major state-owned enterprises suffered a net deficit of M\$1 billion.

By then, Malaysia's fiscal deficit had ballooned to 16 percent of GDP, and the country had generated large volumes of external debt. The Bank offered advice on macroeconomic management, fiscal controls, tax system reforms, and trade reforms aimed at encouraging foreign direct investment. It also advised on state involvement in heavy industry. Macroeconomic adjustment continued from 1986 to 1990, as government policy began emphasizing

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market liberalization and promotion of private sector growth and foreign investment. During this period, too, Malaysia's external debt declined significantly and recourse to external borrowing was reduced in favor of foreign equity funding and domestic borrowing. The ringgit was depreciated to boost manufactured exports. While Malaysia did not require adjustment lending to carry out the World Bank's policy advice, both the Malaysian government and the Bank deemed Bank intervention successful.

Working with the Private Sector in the Philippines

East Asian countries have traditionally relied to a great extent upon market forces. Their development strategies cannot be characterized as *laissez faire*, but they have consistently subjected their industries to international price competition. Their ability to penetrate world markets is an indication of the validity of this strategy. Increasingly, East Asian countries are opening their markets to competition from abroad.

Accompanying a reliance on market forces has been East Asia's dependence on the private sector as the engine of growth. Nonsocialist governments in the region, too, have had public enterprises, but their support for the private sector is older and deeper than it is in other developing regions. Supporting this approach, the Bank has helped provide adequate financing for private sector activities, worked with governments to improve the economic environment, and encouraged governments to increase the range of activities open to the private sector. Formerly socialist economies in East Asia have also recognized the power of the private sector and are now moving, with Bank advice and assistance, to encourage rapid growth in their own private sectors.

Rapid growth has created large demands for infrastructure—especially in power, telecommunications, and transport. But within their fiscal constraints, nations are increasingly unable to finance such demands. Governments have begun to turn to private financiers for

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major projects and to explore innovative forms of project financing and management to accommodate these private interests.

The Philippines, for instance, has led efforts to involve the private sector in a wide range of development activities, particularly infrastructure. Early Bank support included dialogue with the Philippine government to encourage trade reforms and export development. Bank loans have supported such development finance institutions as the Development Bank of the Philippines, as well as improvement in the financial sector.

While the Philippine government is committed to the private sector as a mainstay of development, it has been less successful in providing a stable political and macroeconomic environment or to encourage efficient investment and competition. Consequently, growth did not accelerate in the Philippines as it did in other East Asian countries, and by the mid-1980s, the country's large private debt

burden came to dominate economic policymaking.

The Bank has worked with authorities to redesign policies meant to promote stable growth and to recover from the problems of the 1980s. One Bank-supported activity was a market-oriented debt-relief scheme that the Philippines negotiated with its commercial creditors. Another was a macroeconomic reform program that gave the private sector new confidence to invest in the Philippines. The Bank has also supported policies to improve trade and industrial incentives that resulted in increased foreign and domestic competitiveness. While the Philippines' growth over the past twenty years has not matched that of its neighbors, both the government and the Bank have demonstrated a mutual commitment to overcome particularly difficult economic times that strengthens the basis for future collaboration.

Due in part to difficulties in managing its debt and to the burden that such debt placed on public finances, the

Philippine government has actively sought private sector help in providing infrastructure and public utilities. Since 1989, it has been working with private financiers to carry out build, own, operate and build, own, operate, and transfer projects to produce power for the electricity-starved Philippines economy. Already, thirty-three contracts have been signed and thirteen projects have been completed—greatly reducing power shortages and enabling faster economic growth. The Bank worked with the Philippine government to provide complementary financing for additional power investments, and innovative projects have been started in other sectors as well.

The Philippines now seems to have a solid policy foundation and is moving to restore economic stability and growth. These activities are being followed attentively in other countries in the region. China, Indonesia, Malaysia, and others are inviting more private sector involvement in infrastructure as well as in more traditional areas of production.

China and the Bank: Partners in Transition

While East Asia continues to give high priority to a stable macroeconomy, there are still serious concerns. Socialist economies in transition, such as China and Vietnam, are struggling to maintain stability while they carry out structural reforms and liberalizing price and trade policy. Far-reaching institutional reforms—for example, the restructuring of central banks or revenue and expenditure reassignment between the center and the provinces—are needed. One of the Bank's key tasks will be to bring to the table the best practices in macroeconomic management for socialist economies in transition.

In 1979, after years of little contact with the world economy, China was eager to learn about the policies and experiences of market economies. It made great use of the Bank's accumulated cross-country experience and information on other countries. Even today, after having remarkably accelerated its participation in the world

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The Bank has learned important lessons from its engagement with China. These include lessons of process, of the value of open discussion and debate, and of the need to disseminate ideas to all levels to effect change

economy, China's government remains strongly interested in how other countries address specific economic issues, an interest sustained and stimulated by World Bank economic work.

Chinese leaders have also invited advice from the world's most competent economic analysts. The World Bank's role here has been to gather international experts on China and organize brainstorming seminars with the highest levels of China's economic leadership. These conferences began in the early 1980s and were repeated every two or three years. At last year's conference at Dalian, China confronted several key macroeconomic issues. More specialized conferences have been organized around such specific themes as poverty (1991) and central banking (1993).

The Bank has learned important lessons from its engagement with China. These include lessons of process, of the value of open discussion and debate, and of the need to disseminate ideas to all levels

to effect change. The Bank has also learned from China that where circumstances permit, there are merits in a gradual approach to economic change. China achieved notable progress using this approach in handling price reform, for example. Policymakers adopted a dual-track approach that allowed market prices to coexist with plan prices, while the scope of planned resource allocation was gradually reduced. Today, more than 90 percent of goods in China are at market prices.

China's approach to ownership change has been unusual. It has offered remarkable encouragement to nonstate enterprises, which now account for about half of industrial output. China's gradual but steady strides in other areas—from establishing a land market to giving state enterprises more autonomy; from financial sector reform to adopting sophisticated new markets in commodities and securities—illustrate that, with commitment to change at the highest levels, incremental market reform can work.

China is now among the Bank's most active borrowers. Serious involvement by the Bank began around 1980 with a good deal of basic work in documenting the size and nature of China's newly-opening economy. Operational involvement began with technical assistance loans to finance university education projects and quickly broadened to embrace economic and sector work and continuous monitoring of the Chinese economy. This phase culminated in two major reports on China—one at the beginning of the 1980s and one in 1985. The second report dealt with industry, agriculture, health, and other economic and social aspects of the Chinese economy. It was built around a uniquely designed long-term growth model, which estimated the conditions necessary to meet targets for overall and sectoral growth rates and offered comprehensive recommendations regarding the infrastructure support (social as well as physical) needed to underpin economic growth. Later studies looked at the need for trade liberalization and how China could exploit its comparative advantage in the world economy. Other sectoral studies

examined such issues as revenue mobilization and fiscal reform, financial intermediation, and development of market and distribution systems.

Between 1981 and the end of 1993, the Bank's work in China has been backed by loans of \$9.97 billion and by IDA credits of \$6.97 billion, supporting various investment and technical assistance projects. Conceptually as well as financially, the Bank has supported China's own efforts throughout the transition from a command to a partial-market economy. For example, from the early 1980s the Bank began doing significant work on China's state-owned enterprises and on collectives and small-scale rural enterprises, looking at the kind of changes needed to make them more dynamic and competitive. A series of Bank reports around this time emphasized the need to reduce the number of government plan targets and to increase efficiency and managerial autonomy in state-owned enterprises. Many of the suggested reforms reflected or reinforced ideas already under consideration within China itself.

With commitment to change at the highest levels, incremental market reform can work

Given the size of China's economy, however, the Bank's lending assumes less significance than its technical assistance and economic advice

Given the size of China's economy, however, the Bank's lending assumes less significance than its technical assistance and economic advice. Initially, Bank advice to China initially drew more on the institution's broad experience with East Asian and other developing countries (as well as with industrial countries) than on lessons learned from other socialist economies in transition. In any case, China's economy is more decentralized than other transitional economies. This decentralization has increased with the initiation of economic reforms and center-local fiscal contracting, which builds on the local self-sufficiency and "cellular" structure inherited from the Third Front policies of the Maoist era.

Yet the fundamental problem of dealing with state-owned enterprises remains. Here the Bank has supported China's own strategy to work around the problem rather than to confront it directly, which would be politically risky in terms of unemployment and other social factors (such as health, education, welfare, and housing, for which state-owned

enterprises have traditionally been responsible).

The Bank has supported China's drive to develop collective enterprises to provide employment and produce daily consumer needs. The Chinese government, however, has now widened the scope of its reforms to include price and financial market reform as well as measures aimed at ensuring macroeconomic stability. The need to develop a social-security net, to introduce measures to increase labor market mobility, and to offer better health, education, and housing services has also been central to the Bank's policy advice in China. The aim has been to create an internal market within which change can be introduced. This involves creating competition for state-owned enterprises from collectively owned, town, and village enterprises while encouraging the state-owned entities to contract out more production, a system that has already begun to make Chinese industry more competitive and dynamic. At the same time, the social consequences that accompany changes in the role of state enterprises are being addressed.

Fiscal and financial reforms—more efficient tax collection, equitable to both the center and the provinces—along with the creation of a strong central bank, are two other essential, parallel reforms.

The Bank's dialogue with China has been at the highest political and administrative level and has been characterized by a fruitful exchange of ideas. China has initiated and implemented much of the reform agenda, with the Bank providing guidance and support for what are essentially local initiatives. Chinese leaders listen to what Bank representatives suggest and adapt bank policy or project advice to fit their specific needs. The occasional policy differences—for example, over the relative priority to be given to rural education and health—stand out against a background of mutually rewarding dialogue.

Conclusion

Whatever the level of World Bank involvement in East Asia,

responsibility for the considerable successes of the region rests squarely with the countries themselves. Similarly, the countries have overall responsibility for managing the demanding agenda of the environmental, poverty, infrastructure, and trade issues that will dominate the economic horizon of the twenty-first century. Country commitment and effective policymaking is at the root of economic success—and failure—both now and in the future.

The Bank has had a strong and consistent involvement in East Asia, providing both money and policy and analytical support. The Bank has helped to produce tangible results and has learned valuable lessons, both from the region's considerable achievements and from areas needing much greater attention. But despite the challenges still ahead, one lesson offers considerable encouragement. In East Asia, even daunting tasks have a way of getting done, quietly and efficiently.

In East Asia, daunting tasks have a way of being performed quietly and efficiently

Note

1. Source: Frida Johansen, *Poverty Reduction in East Asia—The Silent Revolution*, World Bank Discussion Paper 203, East Asia Pacific Region Series. This estimate uses individual country poverty lines that are made broadly comparable. Using another common US\$1-per-day poverty line (at purchasing-power parity in exchange rates) yields a 1990 head count estimate for the poor in East Asia of 170 million. No comparable estimates exist for 1970.

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